

# *Implications of the “New” Model of Employer Ascendancy*

**IIR  
Berkeley**



**Sept.  
2005**



**Daniel J.B. Mitchell  
and**



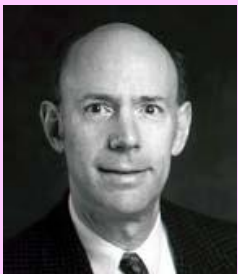
**Christopher L. Erickson**

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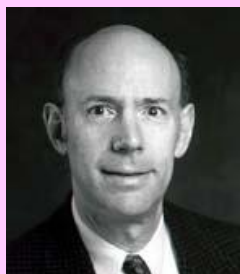
**Christopher L. Erickson**

# *Implications of the “New” Model of Labor-Market Monopsony*

**IIR  
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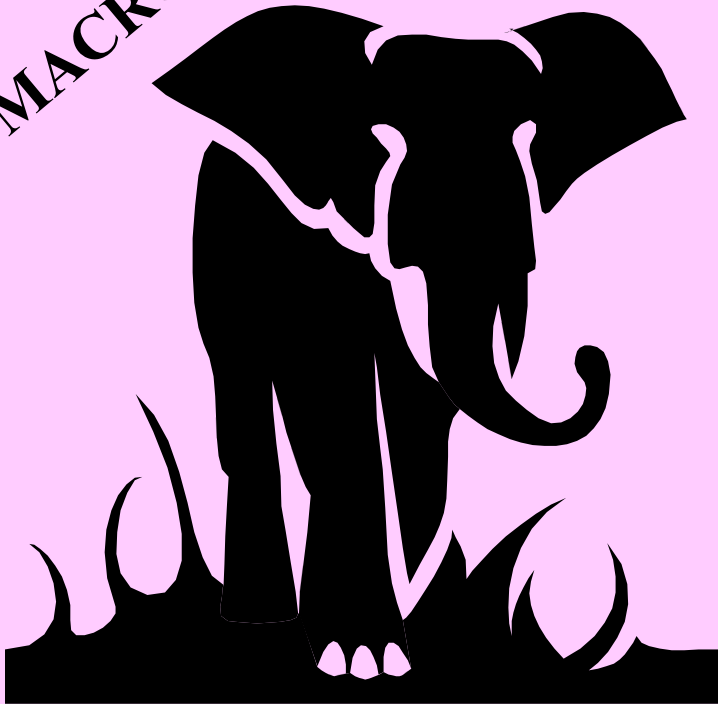


**Christopher L. Erickson**

**Time to re-think our understanding  
of how the “new” (largely nonunion)  
labor market functions...**



**MACRO**



**micro**



**...both at the macro and  
micro levels.**

# *Monopoly*



**Seller Power**



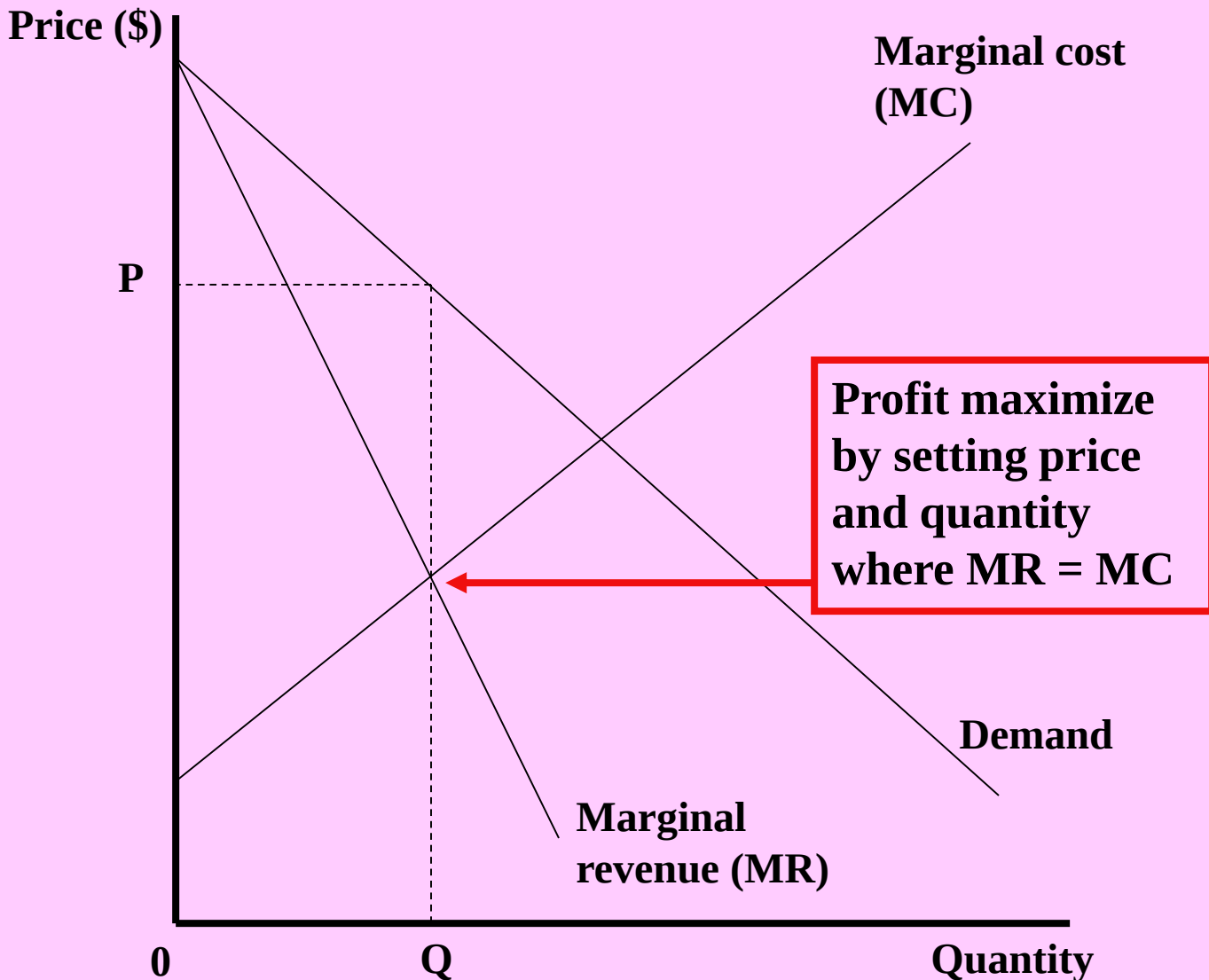


# *Monopoly*



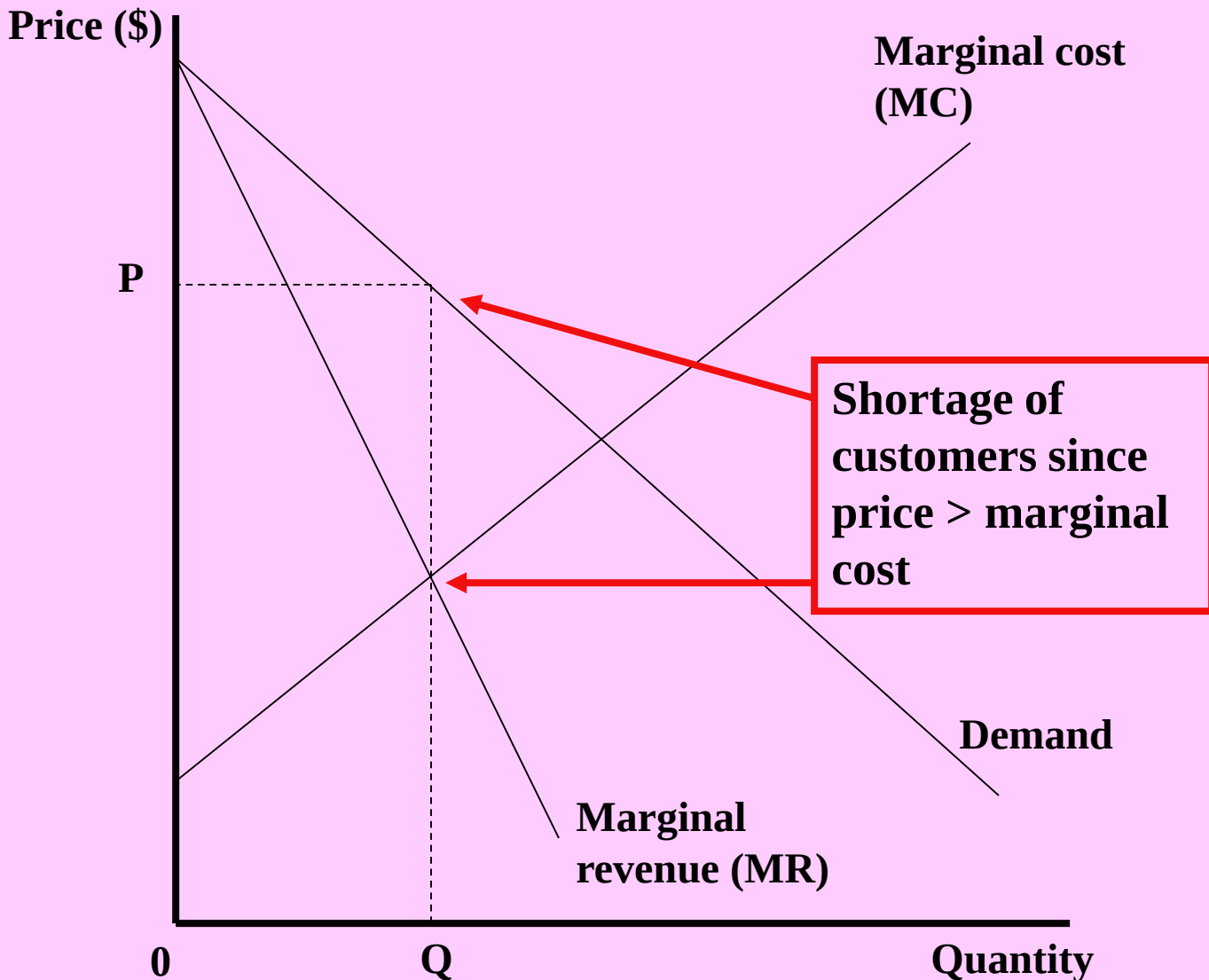
**Byproduct is “shortage”  
of customers because  
price is “too” high**

# *Monopoly*



**Byproduct is “shortage”  
of customers because  
price is “too” high**

# *Monopoly*



**Byproduct is “shortage”  
of customers because  
price is “too” high**



**"Use RCA RADIOTRONS"**  
—say leading radio builders



Vacuum tubes are the heart of your radio set. Sensitivity, selectivity and tone depend on their quality. Your set—whatever its make—was designed by the manufacturer to give you best performance with RCA Radiotrons. These tubes are the acknowledged standard of the industry—easy to buy, easy to use, easy to replace. Don't handicap a good radio set with inferior, shoddy tubes that call for frequent repairs and produce distorted notes.

Look for the red and black tubes and the famous RCA trade mark.

Manufacturers with a reputation to maintain use the tubes with a reputation back of them.

General Electric, Philips, Thomsen & Edison, Inc., etc. "When choosing tubes to build, we use the performance of tubes standing out with RCA Radiotrons. We do this because the RCA tube is a product of tubes we are proud. In our products we never sacrifice reliability for our interests, we insist on the best RCA Radiotrons for the value, appearance and for replacement."

**RCA Radiotron**  
THE HEART OF YOUR RADIO SET

# Monopoly



P



Shortage of customers since  
 $\text{price} > \text{marginal cost}$

Demand

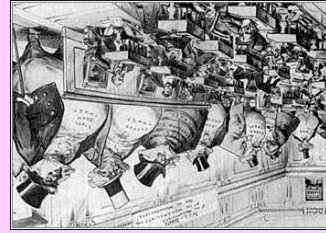
0



Quantity

Byproduct is “shortage”  
of customers because  
price is “too” high

**Monopsony is flip side of Monopoly:**  
***It is buyer (employer) power rather  
than seller power.***



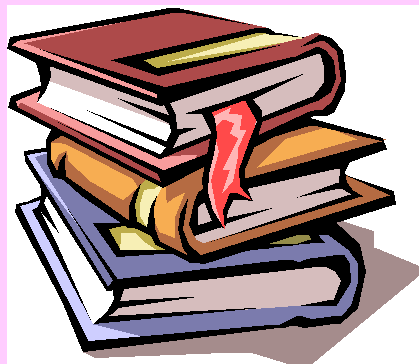
**Byproduct is “shortage” of  
workers (to rent) because  
price (wage) is too low**

**Monopsony is flip side of Monopoly:**  
*It is buyer (employer) power rather  
than seller power.*

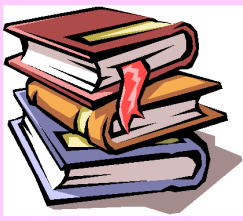


**Byproduct is “shortage” of  
workers (to rent) because  
price (wage) is too low**

**Monopsony:**  
***It's not just for nurses  
anymore!!***







*...or just for isolated  
coal mining towns*



**Company  
store**

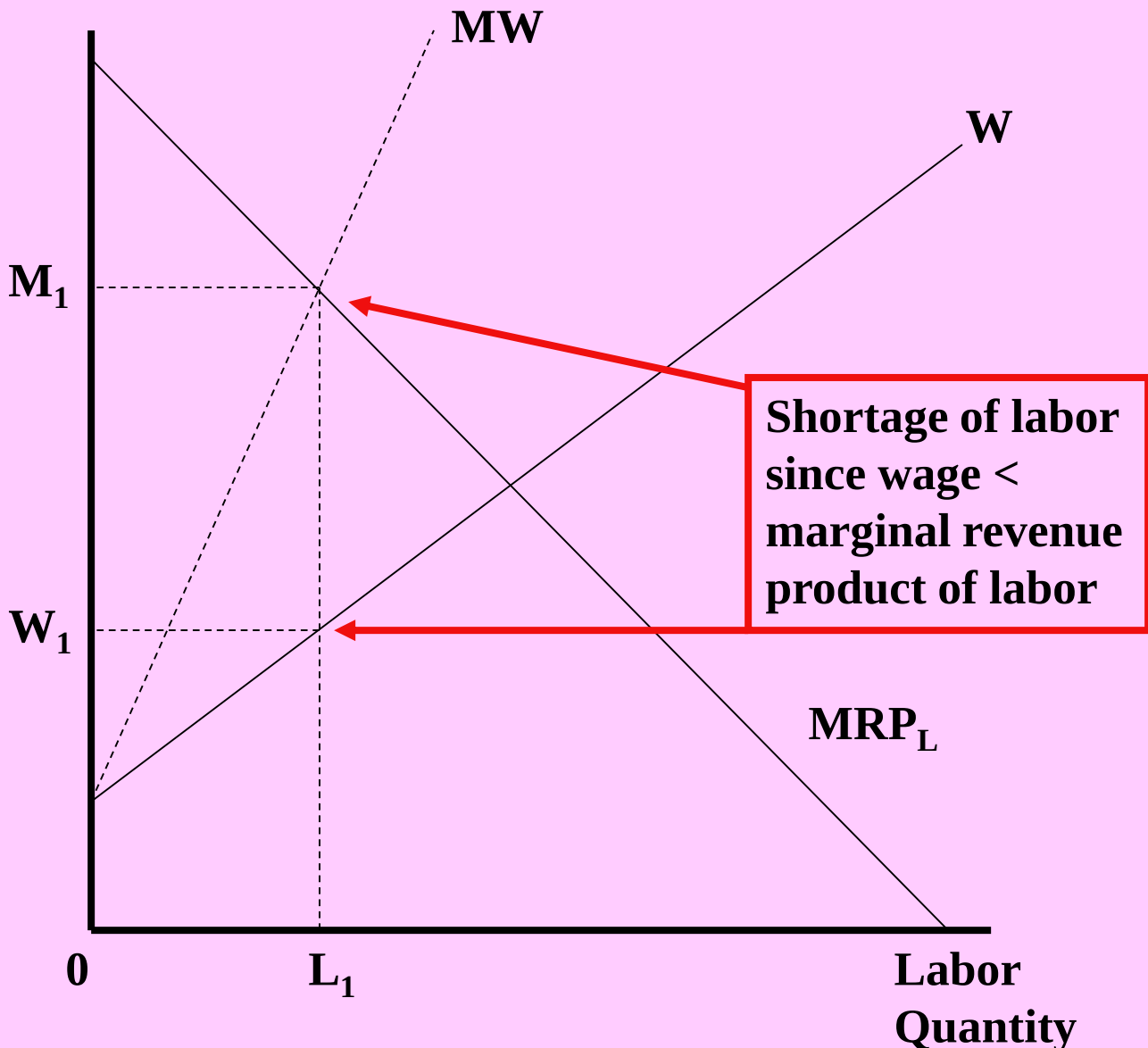
**Company  
town**



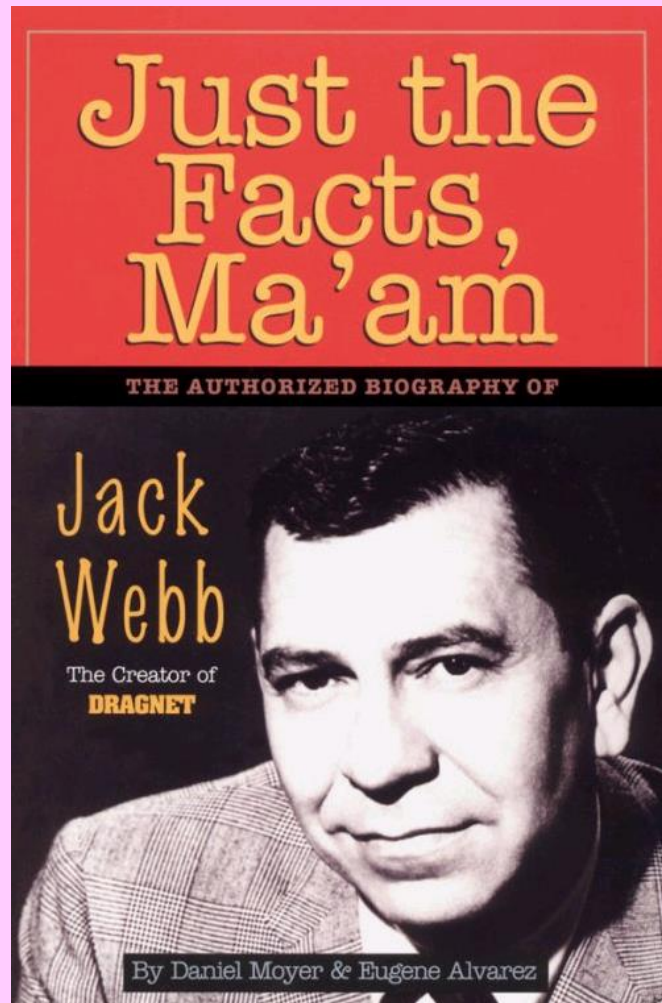
**(late 19th century)**



# Standard Labor Market Monopsony Analysis







# Stylized Facts



- **Declining unions**
- **Labor shortages in late 1980s and 1990s**
- **Growth in income inequality**
- **Real wage slowdown**
- **Surprisingly low unemployment in late 1990s**
- **Stagnating participation rate recently**
- **Recessions in the early 1990s and early 2000s mild relative to 1970s and 1980s**

# Mitchell-Erickson Monopsony



Approach Explains:



- **Labor shortages**
- **Mild recessions**
- **Low unemployment**
- **And other stylized facts...**

*...without relying on  
new economy,  
globalization,  
technology, and other  
popular explanations*

# **Note: *A Work in Progress***



Comments and  
suggestions welcome

# Still loose ends

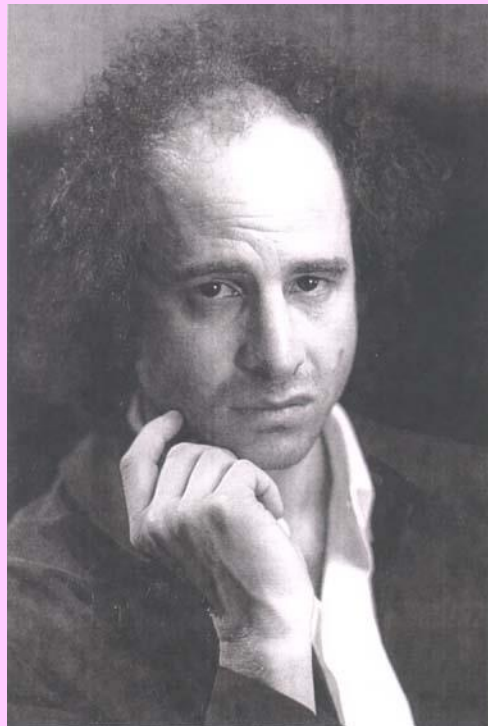


**Not a theory of everything** •



**“You can’t have  
everything. Where  
would you put it?”**

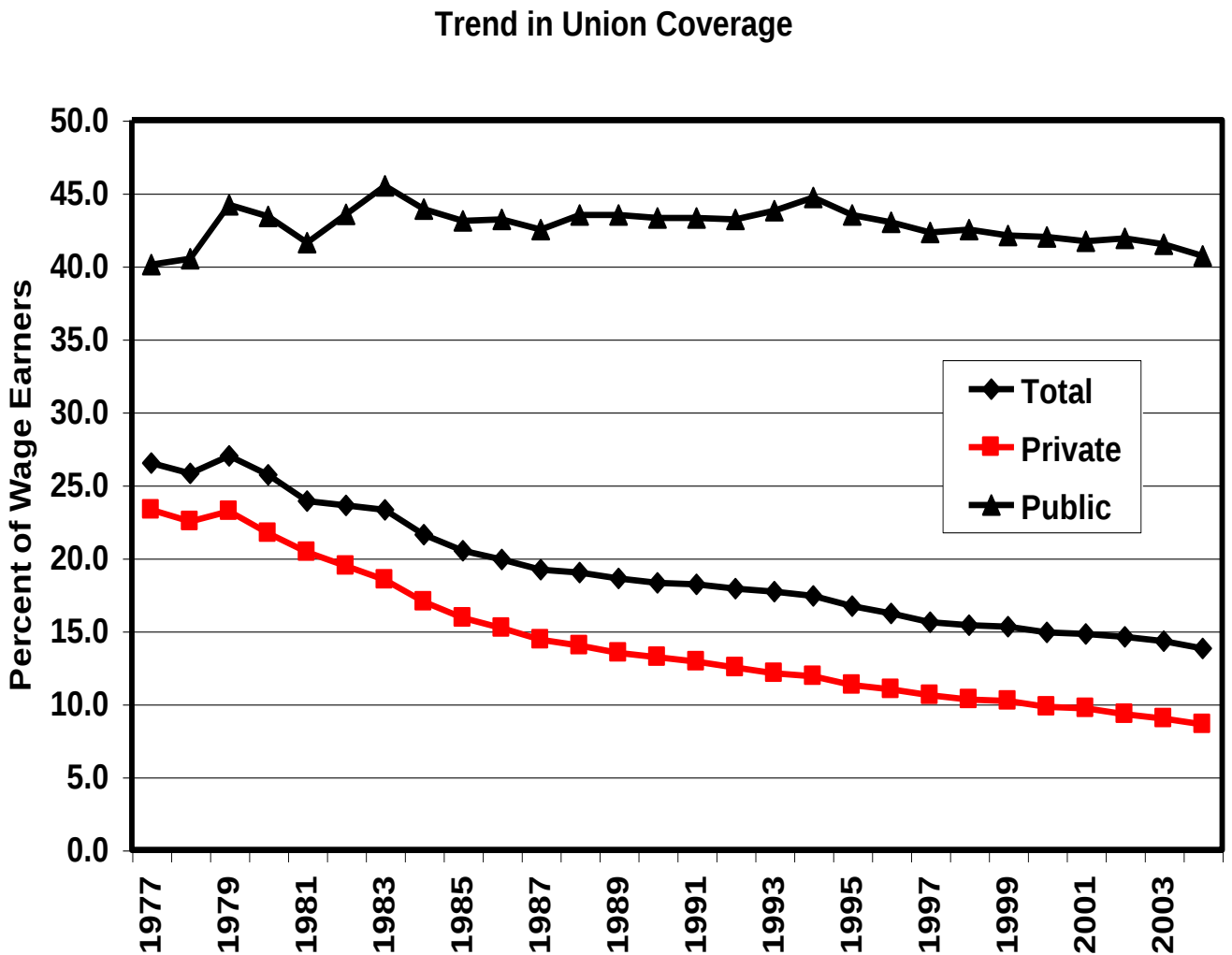
*Stephen Wright*



# Stylized Facts



- Declining unions



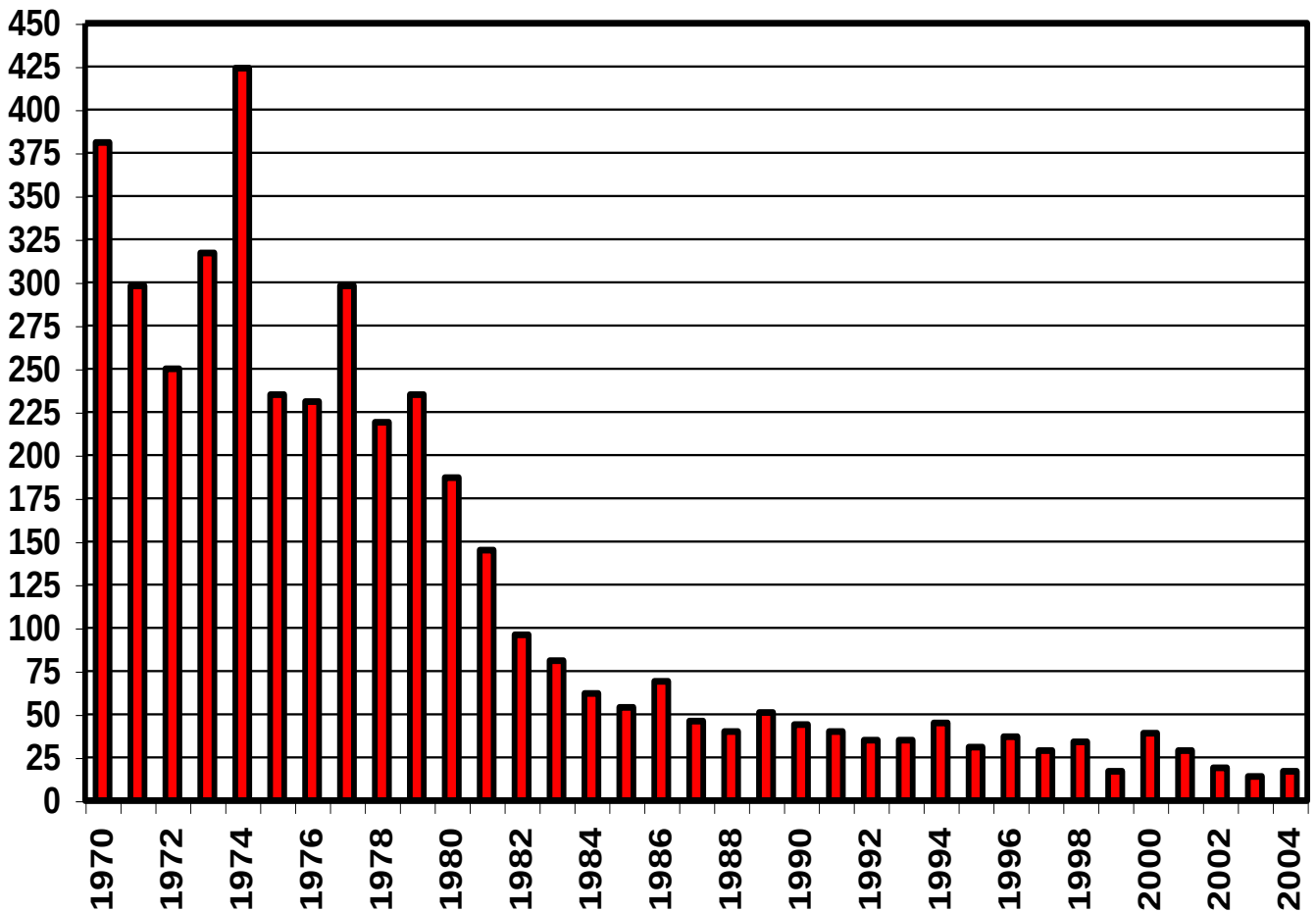
CPS via Hirsch & Macpherson

# Stylized Facts



- Declining unions

Number of Major Work Stoppages



BLS

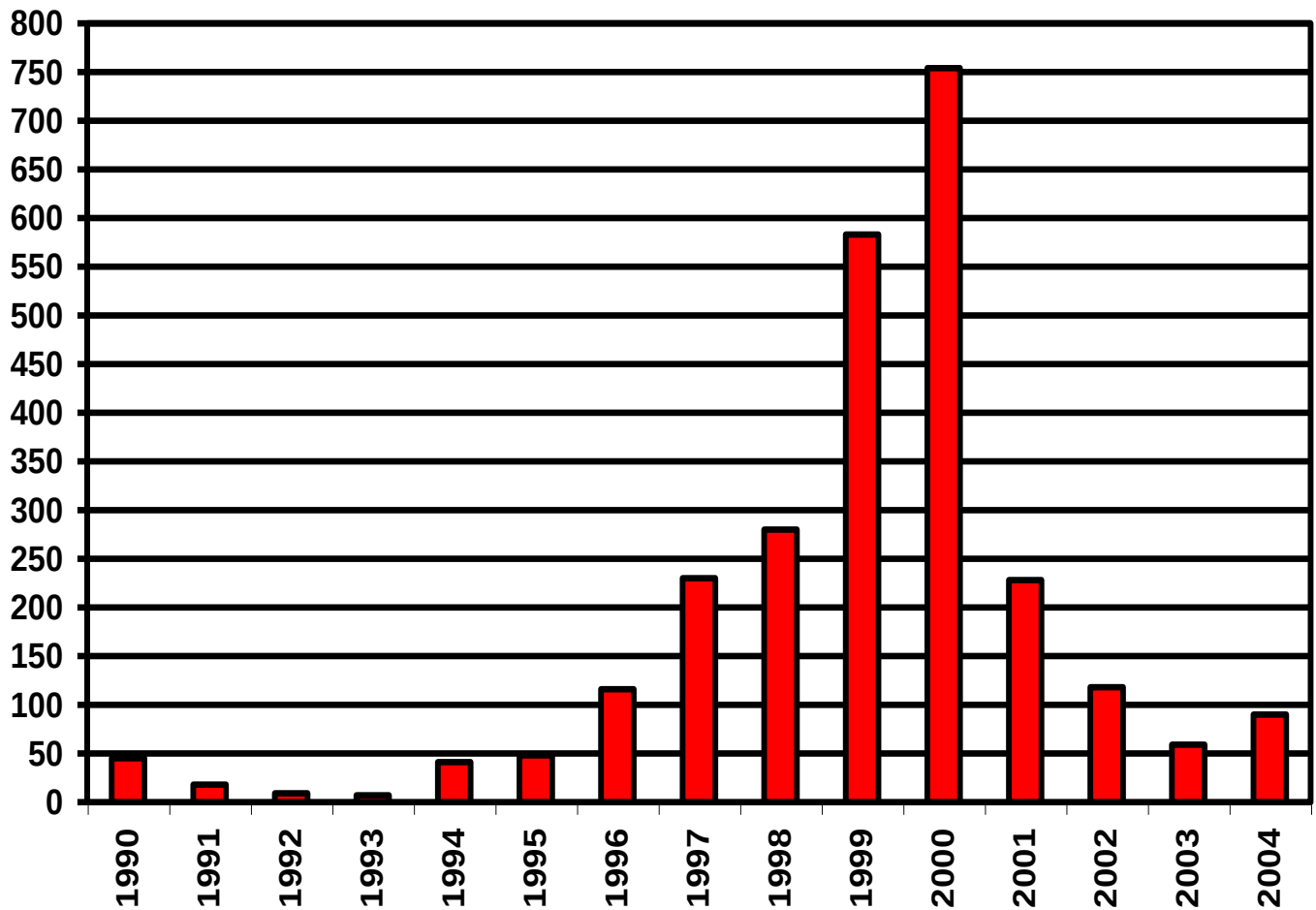


# Stylized Facts



- Labor shortages in late 1980s and 1990s

Nexis/Lexis "Regnws" Labor Shortages Citations



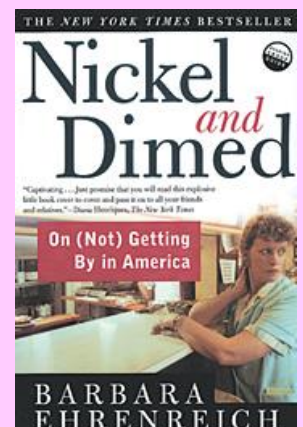
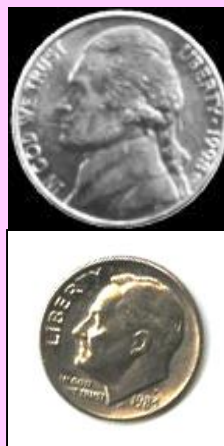
Preliminary: One month per quarter

Mar., Jun., Sept., Dec.

***“... (T)he want ads are not a reliable measure of the actual jobs available at any particular time. They are ... the employers’ insurance policy against the relentless turnover of the low-wage workforce. Most of the big hotels run ads almost continuously, if only to build a supply of applicants to replace the current workers as they drift away or are fired, so finding a job is just a matter of being in the right place at the right time and flexible enough to take whatever is being offered that day.”***

**Barbara Ehrenreich**

## **Nickel and Dimed**



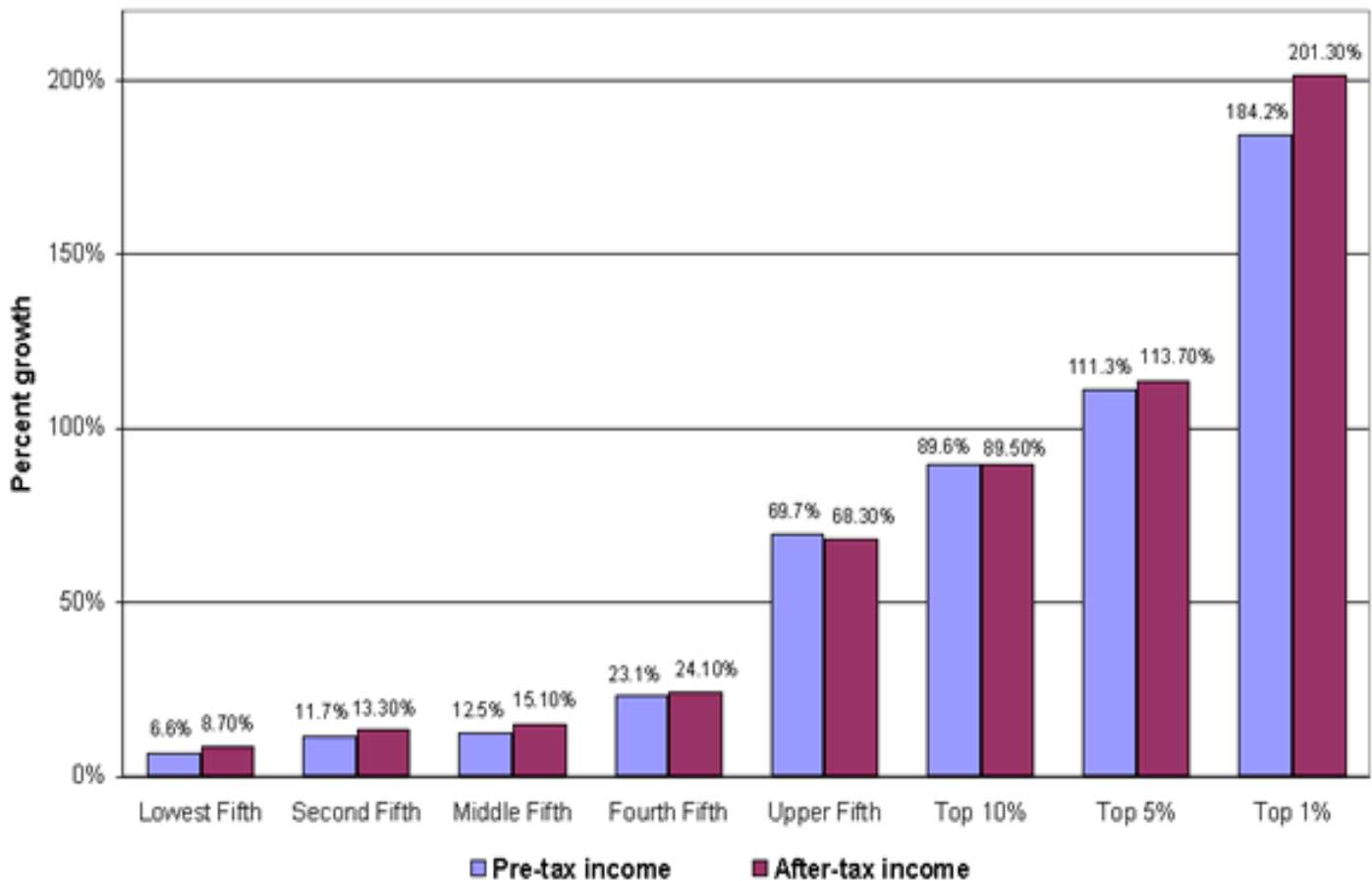


# Stylized Facts



- Growth in income inequality

Growth in real household pre-tax and after-tax income, 1979-2000



Source: Author's analysis of Congressional Budget Office data.

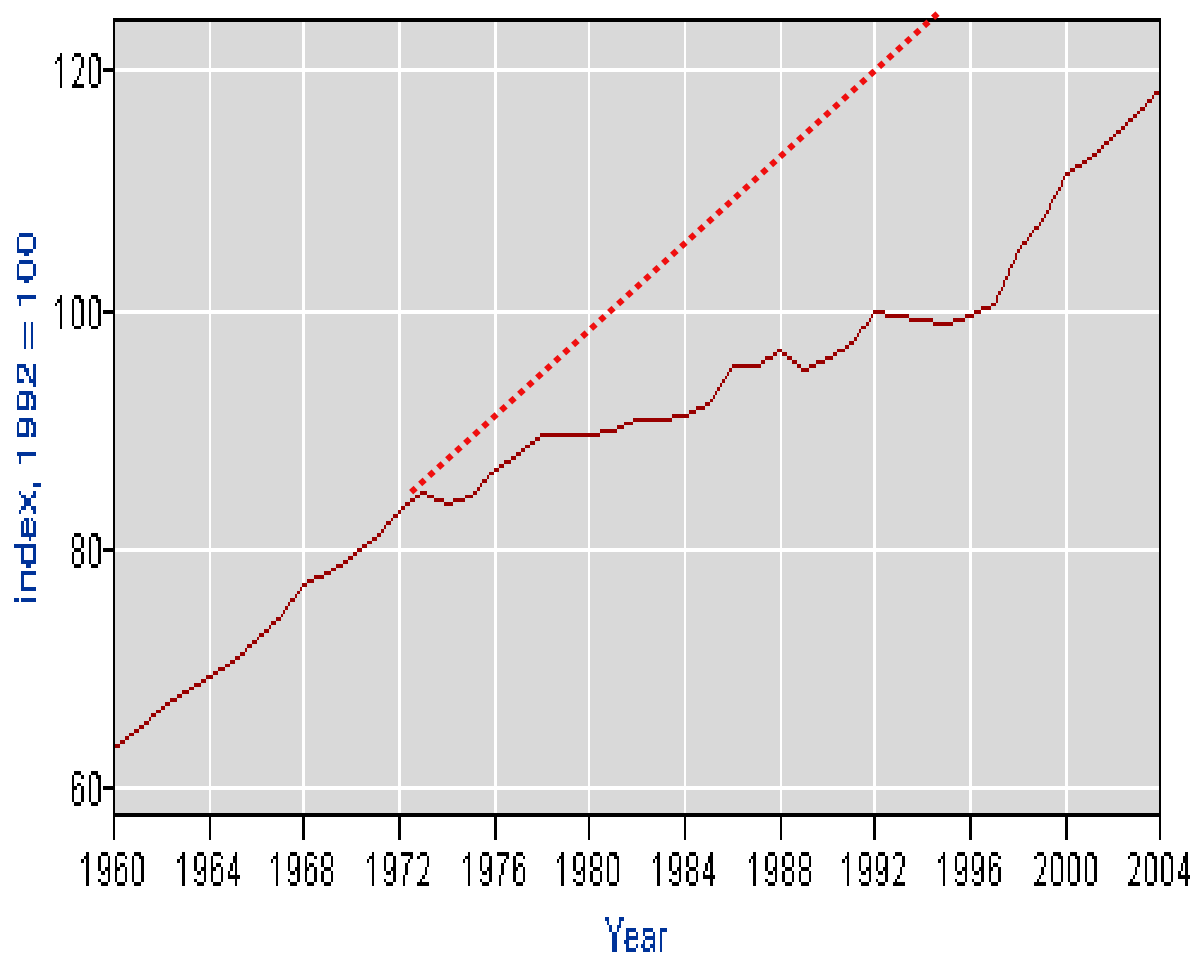


# Stylized Facts



- Real wage slowdown

## Real Nonfarm Hourly Compensation



**BLS**



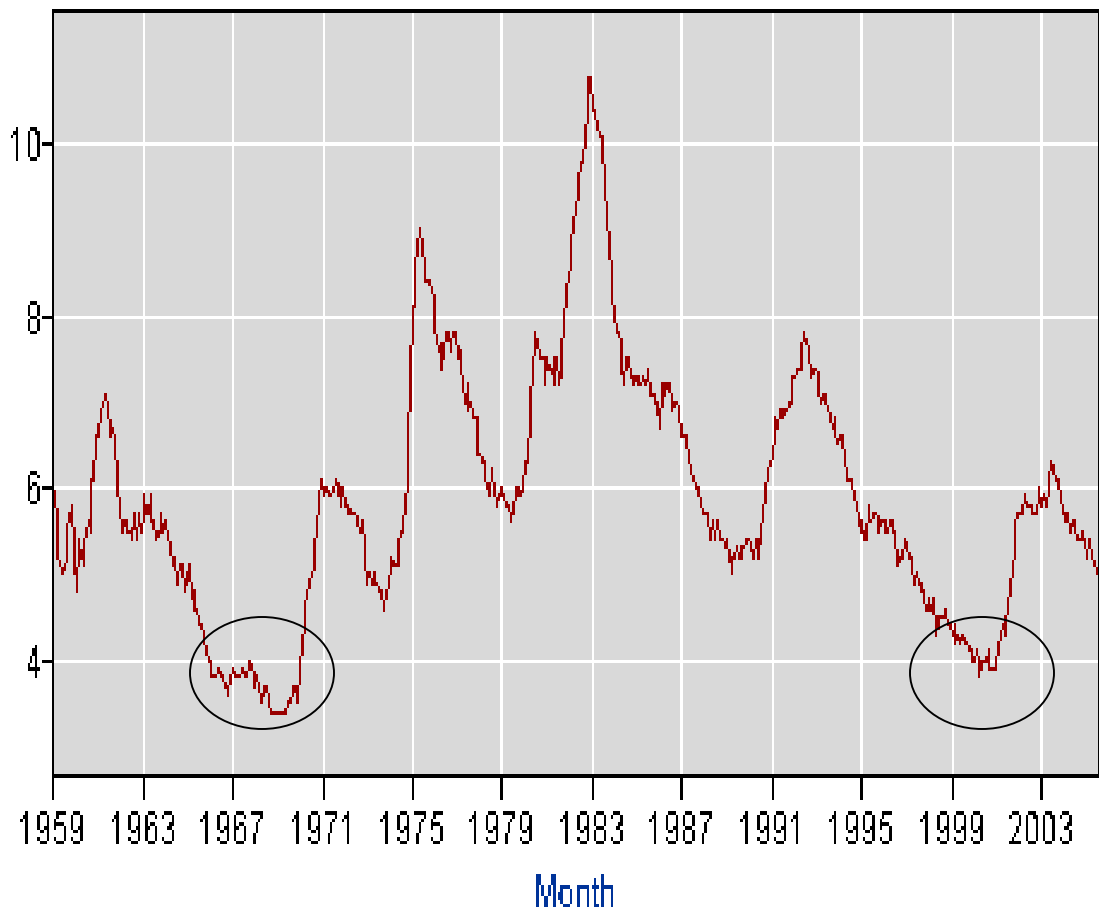
**"Before I forget, Detrick, here's the dental plan."**

# Stylized Facts



- Surprisingly low unemployment in late 1990s

## Unemployment Rate



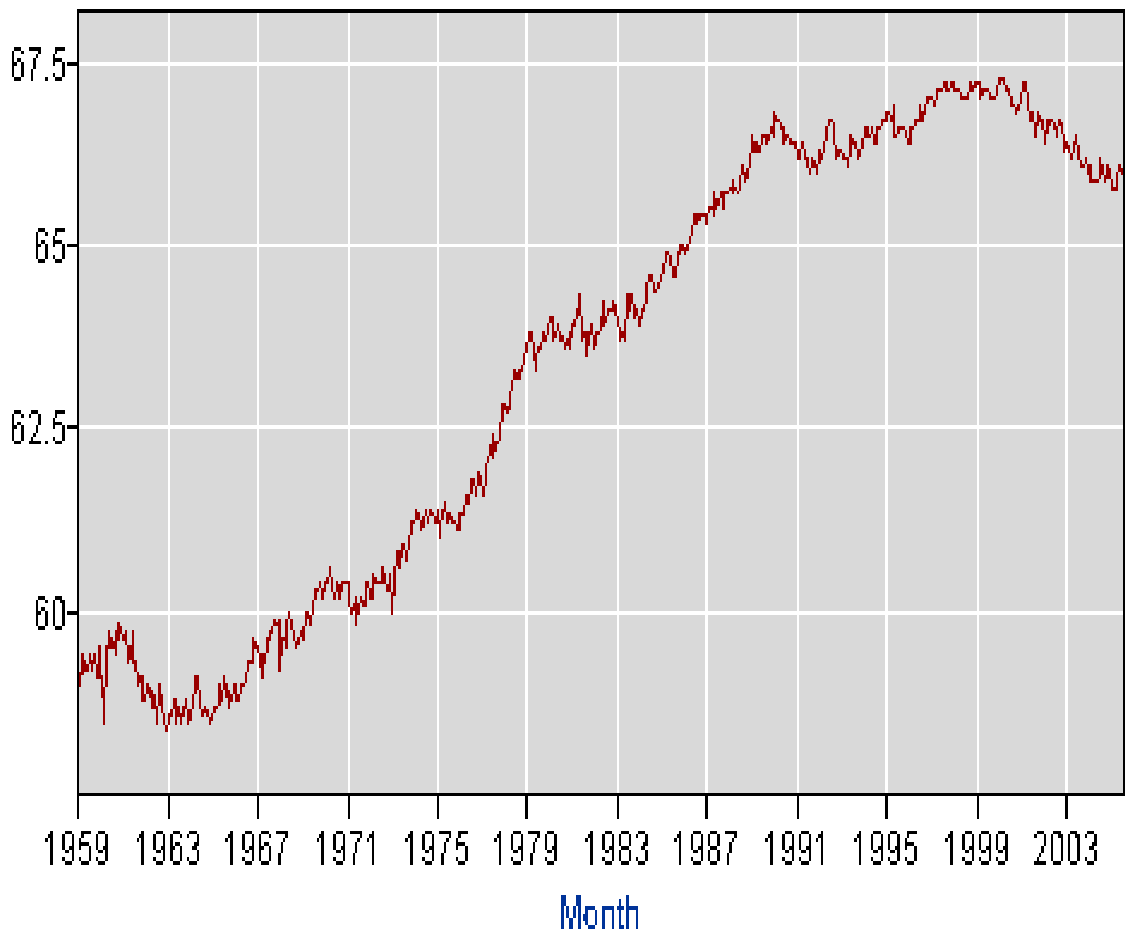
**BLS**

# Stylized Facts



- **Stagnating participation rate recently**

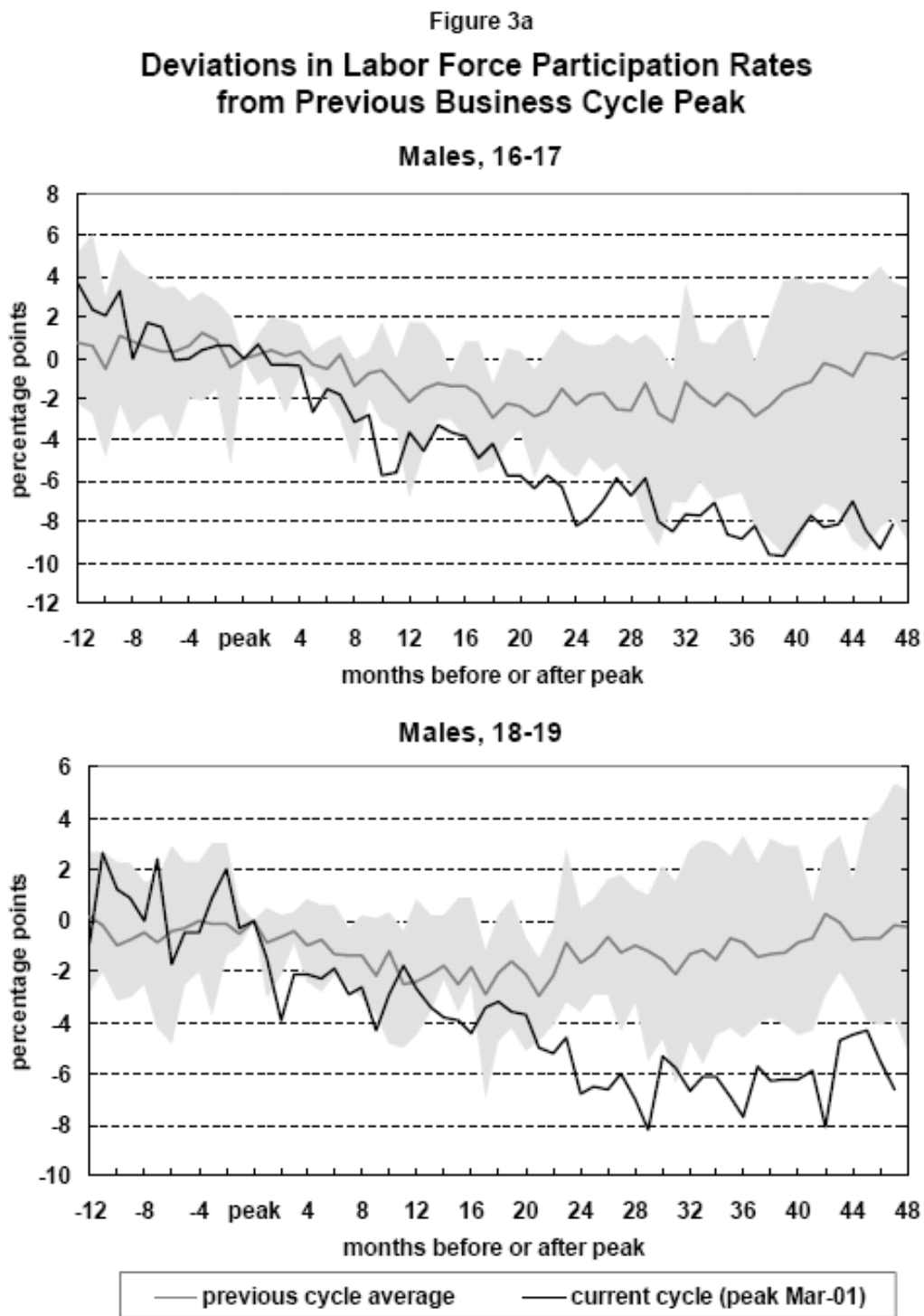
## Civilian Participation Rate



**BLS**

*(perhaps people don't want the jobs that are available)*





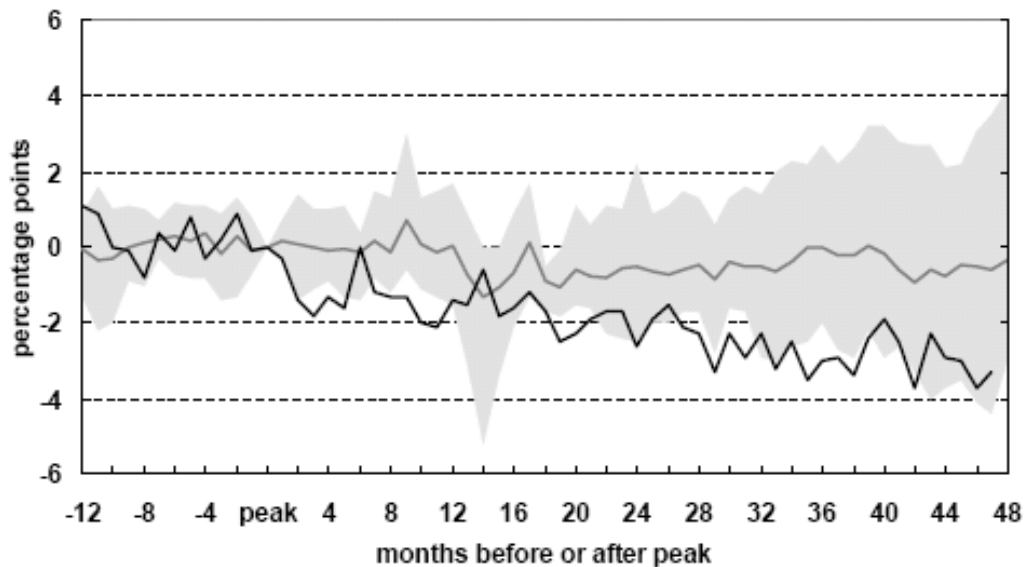
Note: Shading indicates range of values in five previous recessions.

**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**

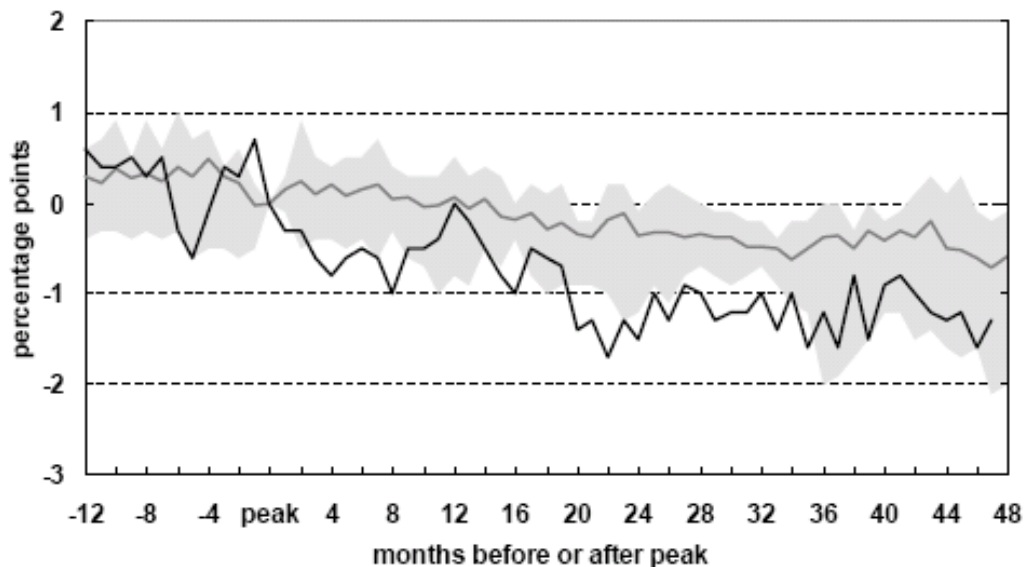
Figure 3b

### Deviations in Labor Force Participation Rates from Previous Business Cycle Peak

Males, 20-24



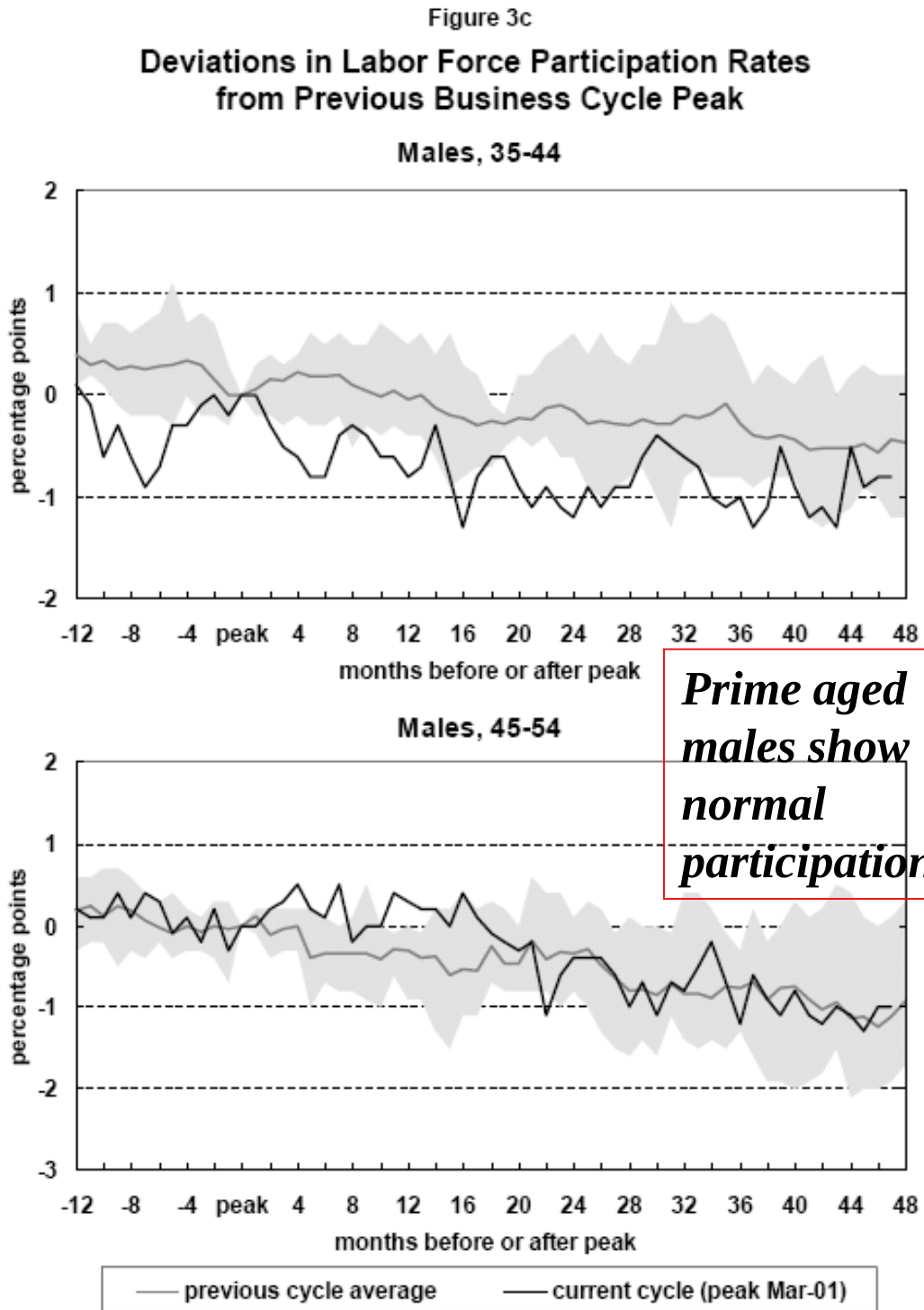
Males, 25-34



— previous cycle average      — current cycle (peak Mar-01)

Note: Shading indicates range of values in five previous recessions.

**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**



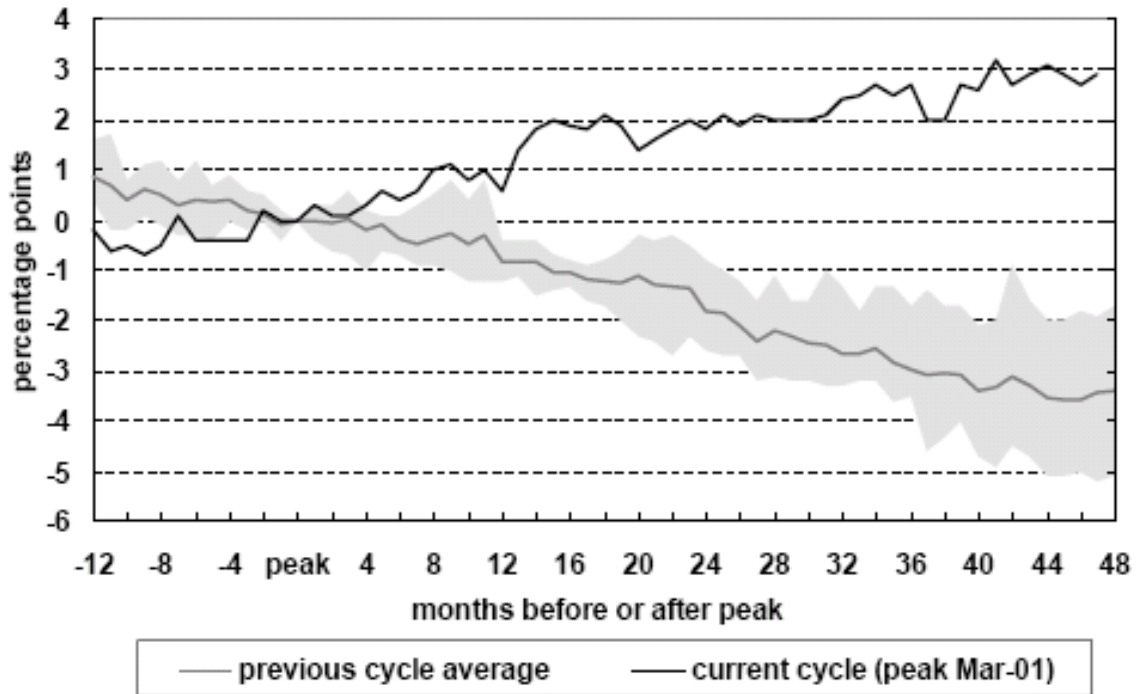
Note: Shading indicates range of values in five previous recessions.

**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**

Figure 3d

### Deviations in Labor Force Participation Rates from Previous Business Cycle Peak

Males, 55+



Note: Shading indicates range of values in five previous recessions.



**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**



***Board Chair  
Kenneth Lay***



***CEO Jeff Skilling***



***CFO Andrew Fastow***

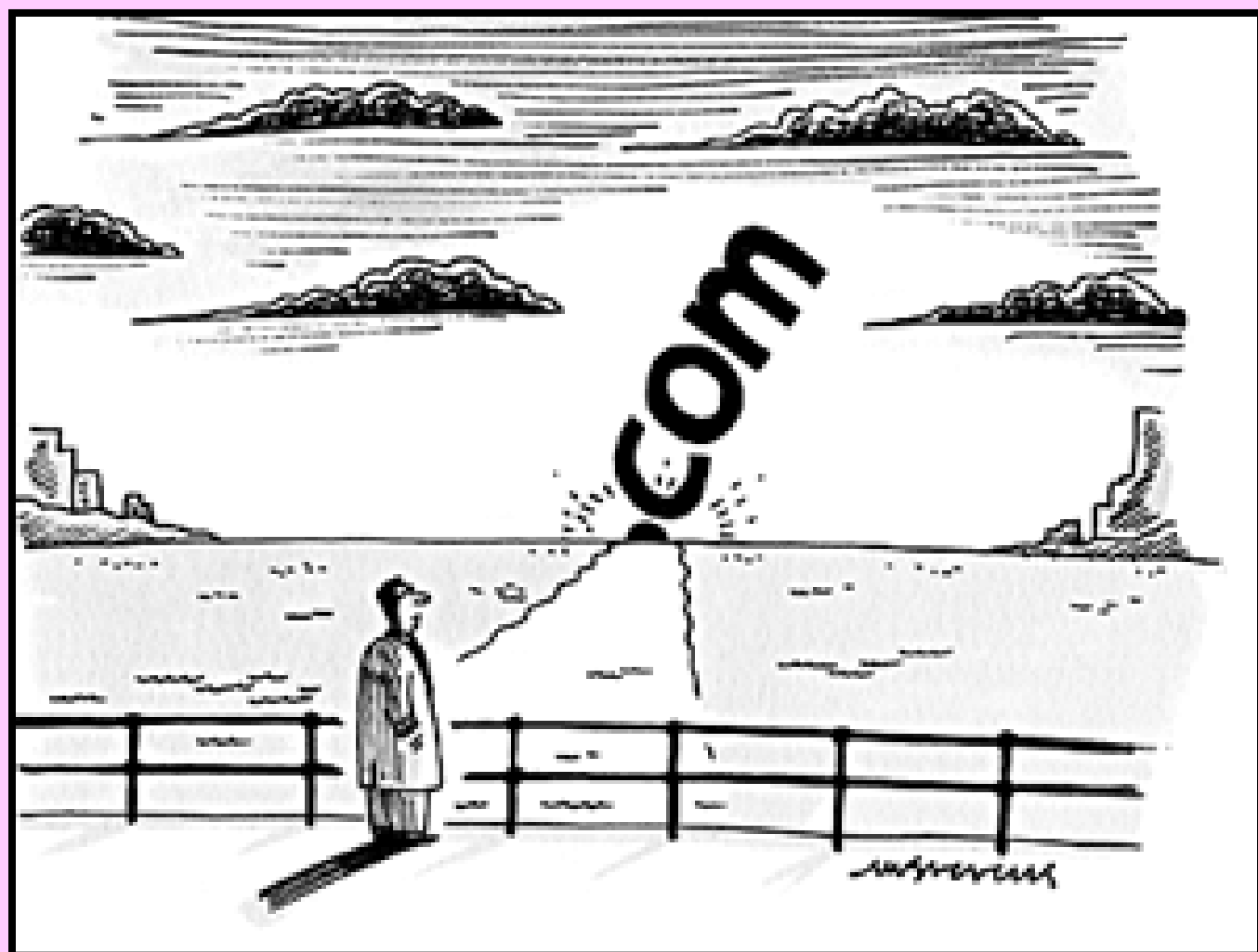
# *A thought from Skilling's mom*



**“When you are the CEO  
and are on the Board of  
Directors, you are  
supposed to know what’s  
going on with the rest of  
the company.”**

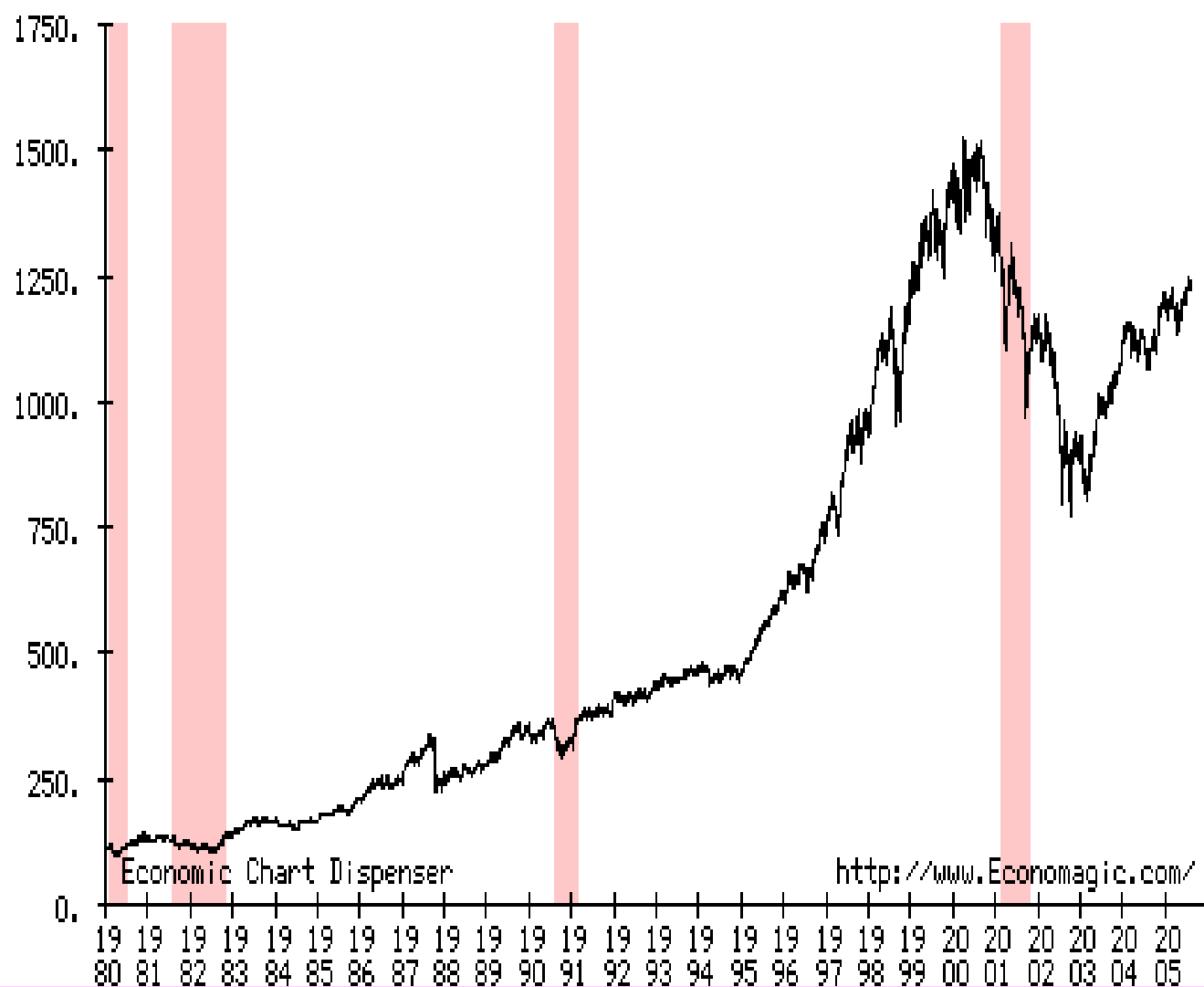
**---Betty Skilling**

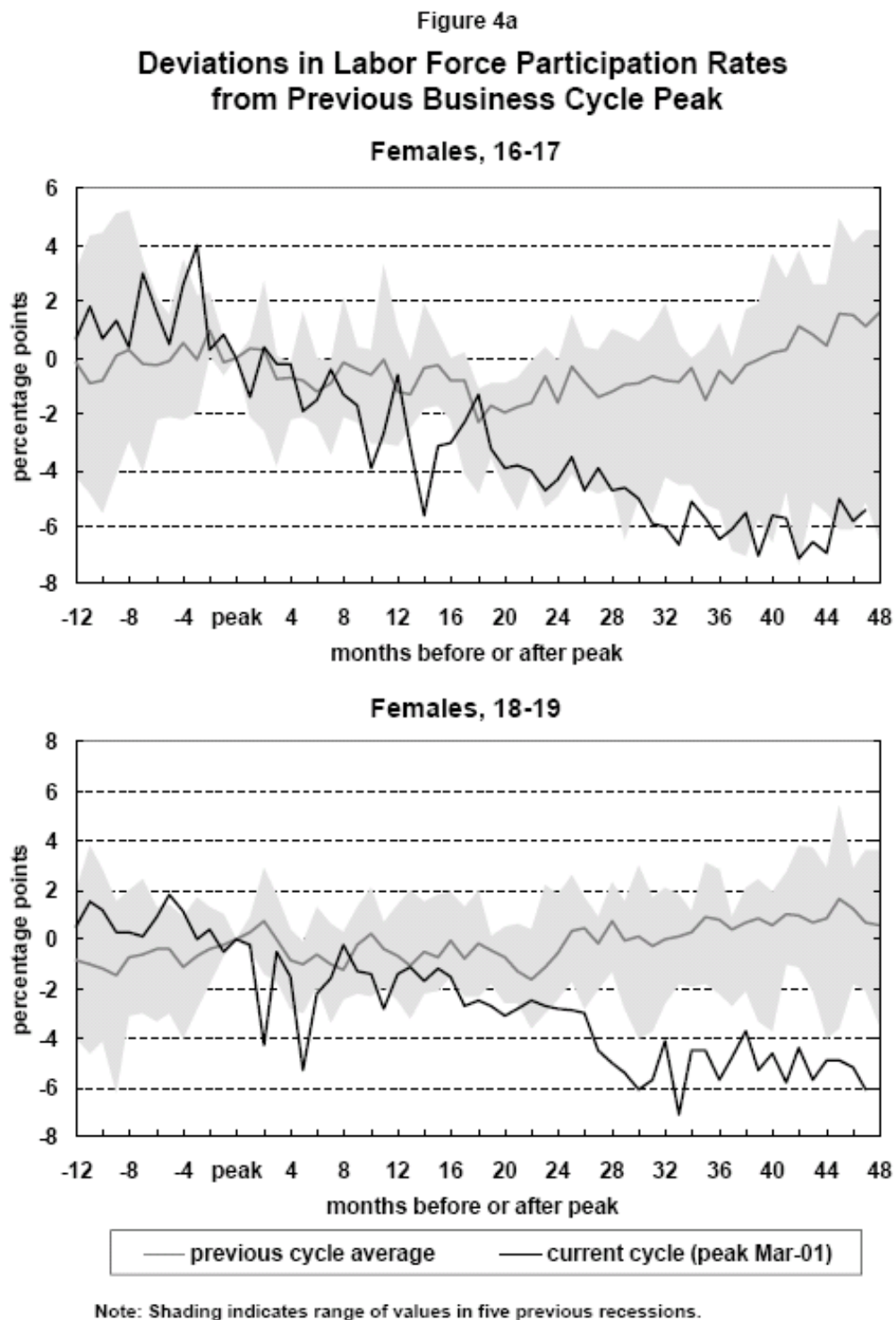






## S&P 500: Close



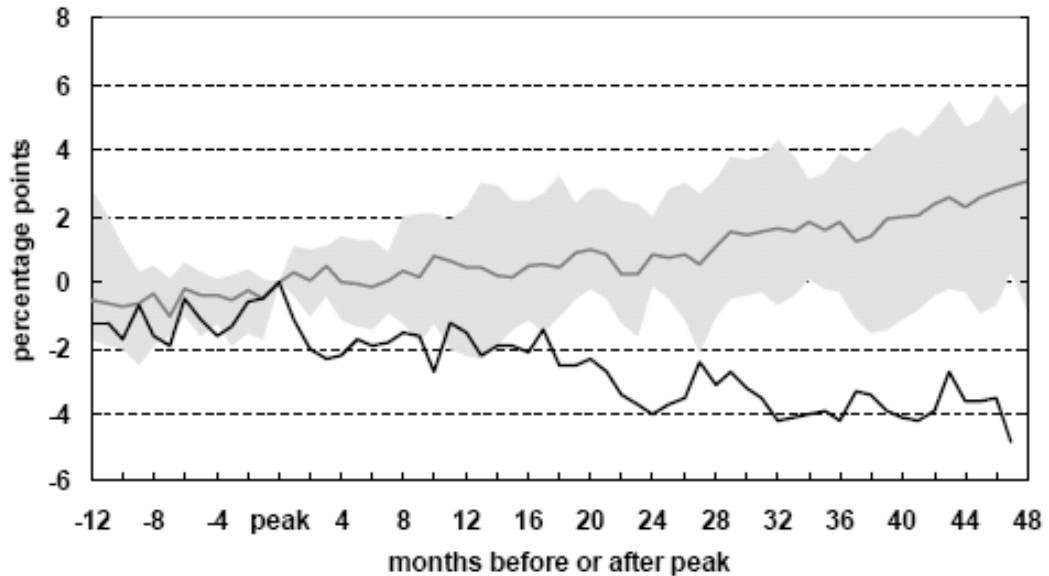


**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**

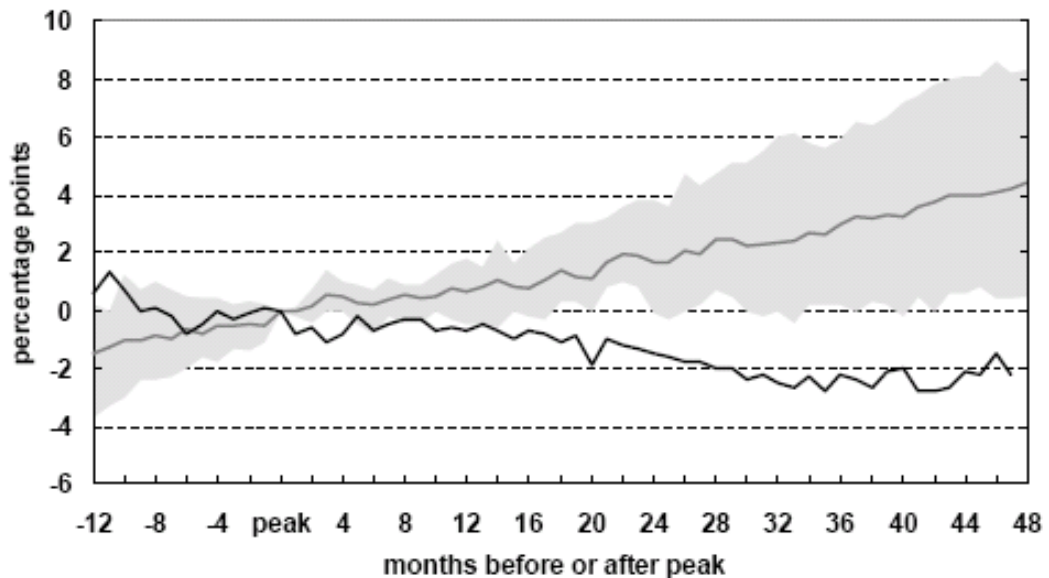
Figure 4b

## Deviations in Labor Force Participation Rates from Previous Business Cycle Peak

Females, 20-24



Females, 25-34



— previous cycle average      — current cycle (peak Mar-01)

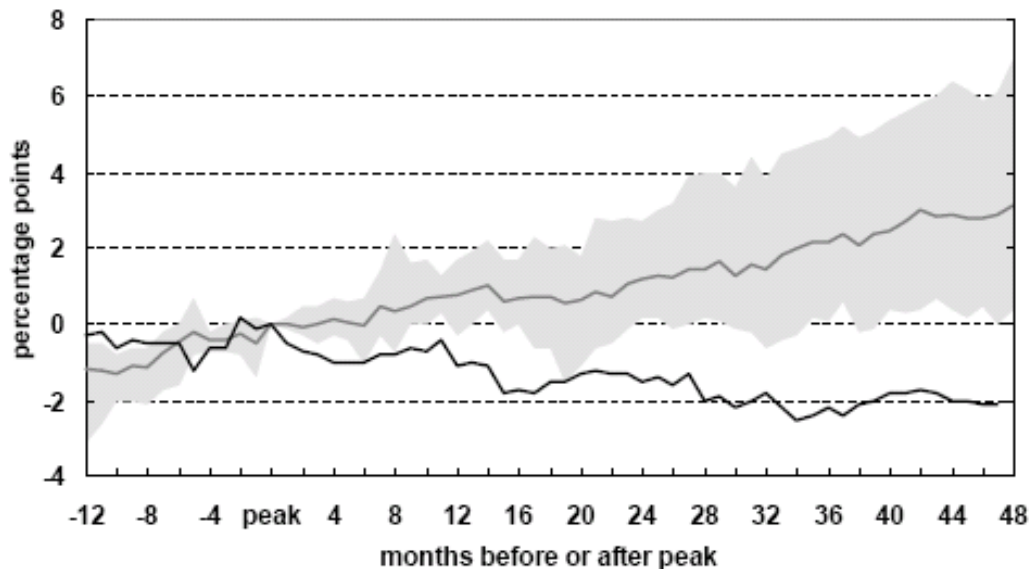
Note: Shading indicates range of values in five previous recessions.

**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**

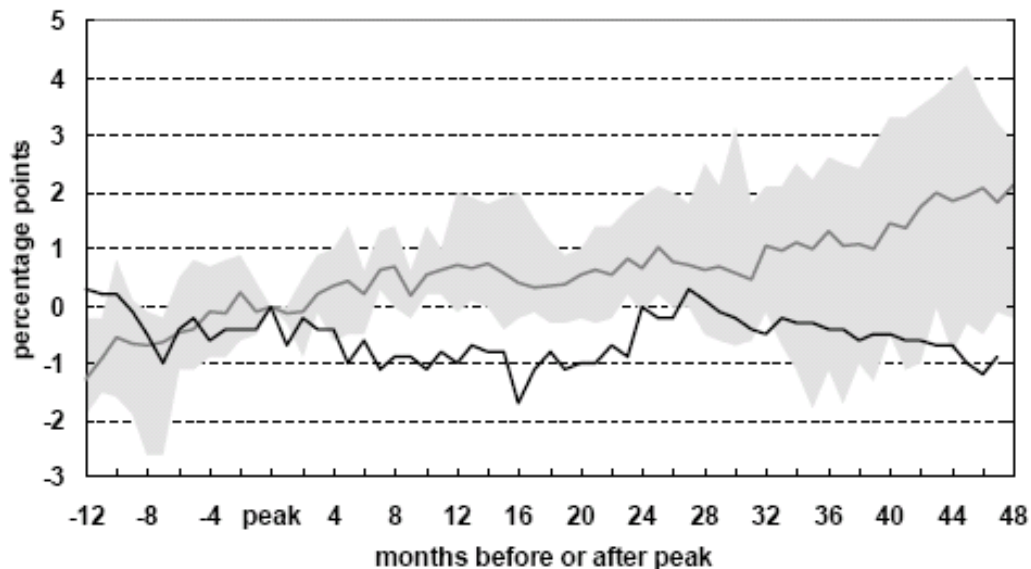
Figure 4c

### Deviations in Labor Force Participation Rates from Previous Business Cycle Peak

Females, 35-44



Females, 45-54



— previous cycle average      — current cycle (peak Mar-01)

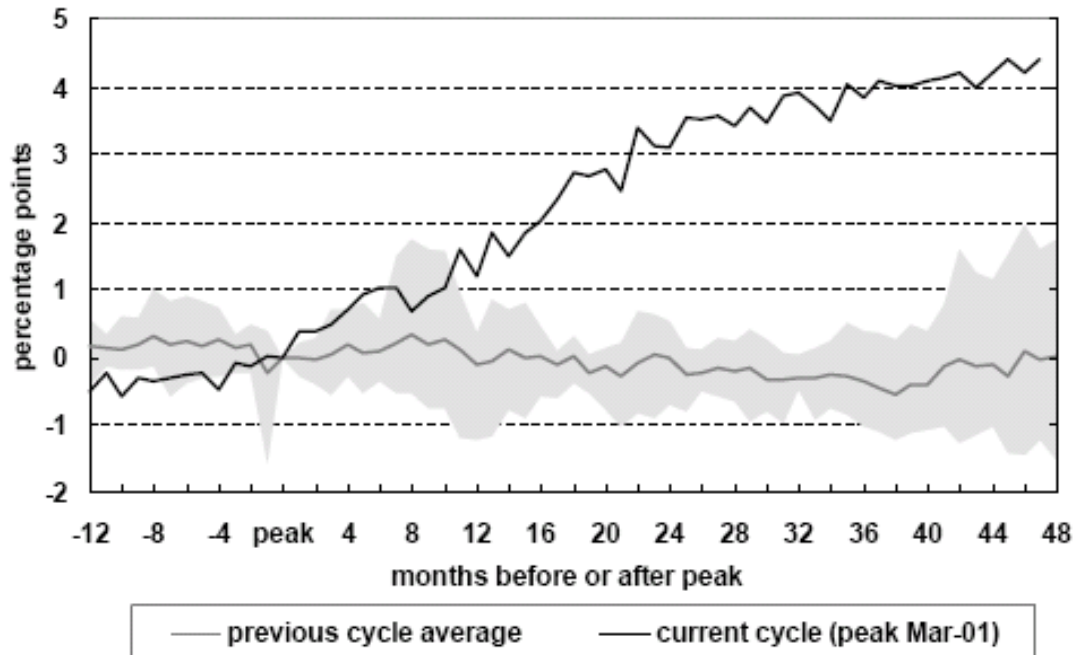
Note: Shading indicates range of values in five previous recessions.

**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**

Figure 4d

### Deviations in Labor Force Participation Rates from Previous Business Cycle Peak

Females, 55+



Note: Shading indicates range of values in five previous recessions.



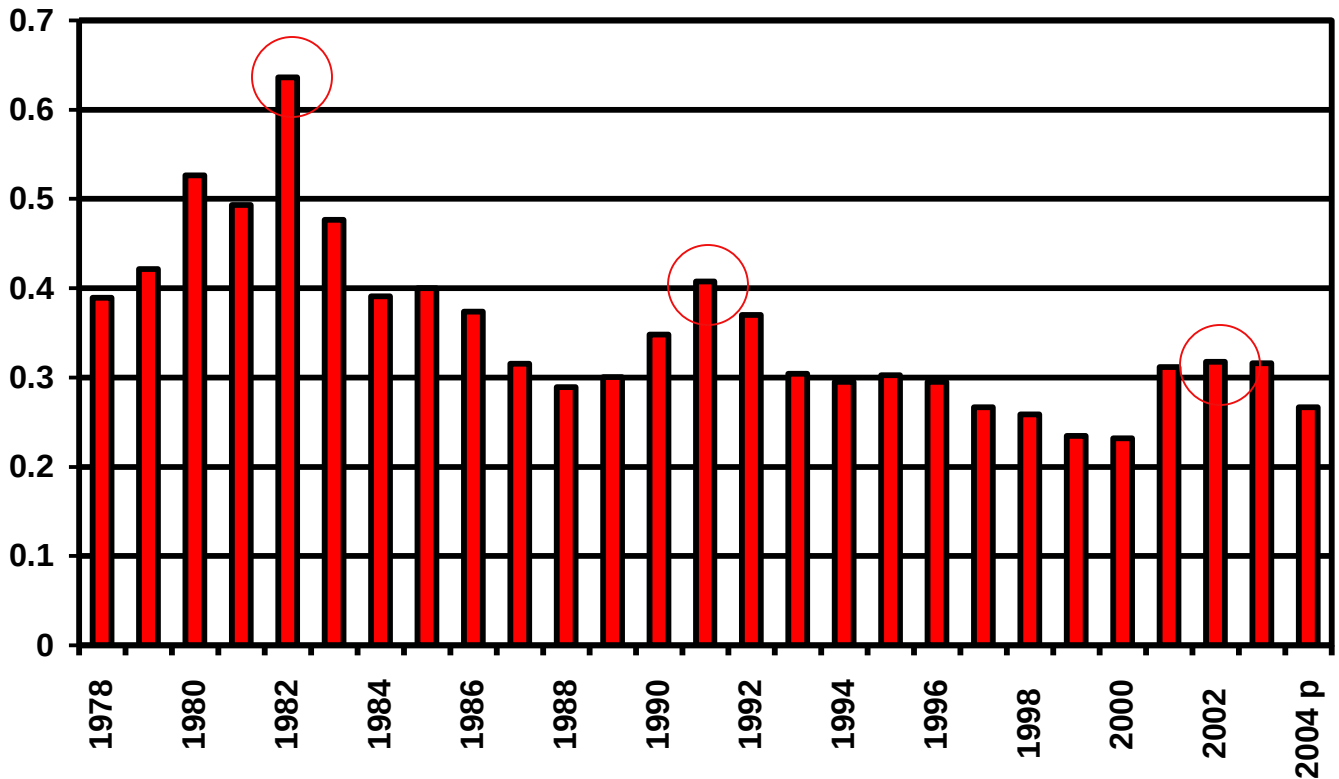
**Source: Katharine Bradbury: “Additional Slack in the Economy: The Poor Recovery in Labor Force Participation During this Business Cycle,” Fed Res Bank of Boston, Policy Brief 05-2, July 2005**

# Stylized Facts



- Recessions in the early 1990s and early 2000s mild relative to 1970s and 1980s

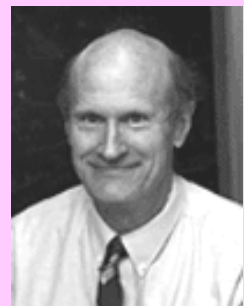
Average Weekly New UI Claims as Percent of Covered Employment



(not a lot of layoffs recently)

*Let's make sense of the stylized facts by calling upon work of some well-known economists*

- ❑ **Richard Freeman**
- ❑ **James Medoff**
- ❑ **Martin Weitzman**
- ❑ **David Card**
- ❑ **Alan Krueger**
- ❑ **Truman Bewley**





# *Let's even bring in Alan Greenspan*

5/30/91 A14  
LOS ANGELES TIMES



Arsene Studio

Henry Jerome Band performing in New York City in 1945 with Alan Greenspan, saxophone, at far left.

and his  
colleagues



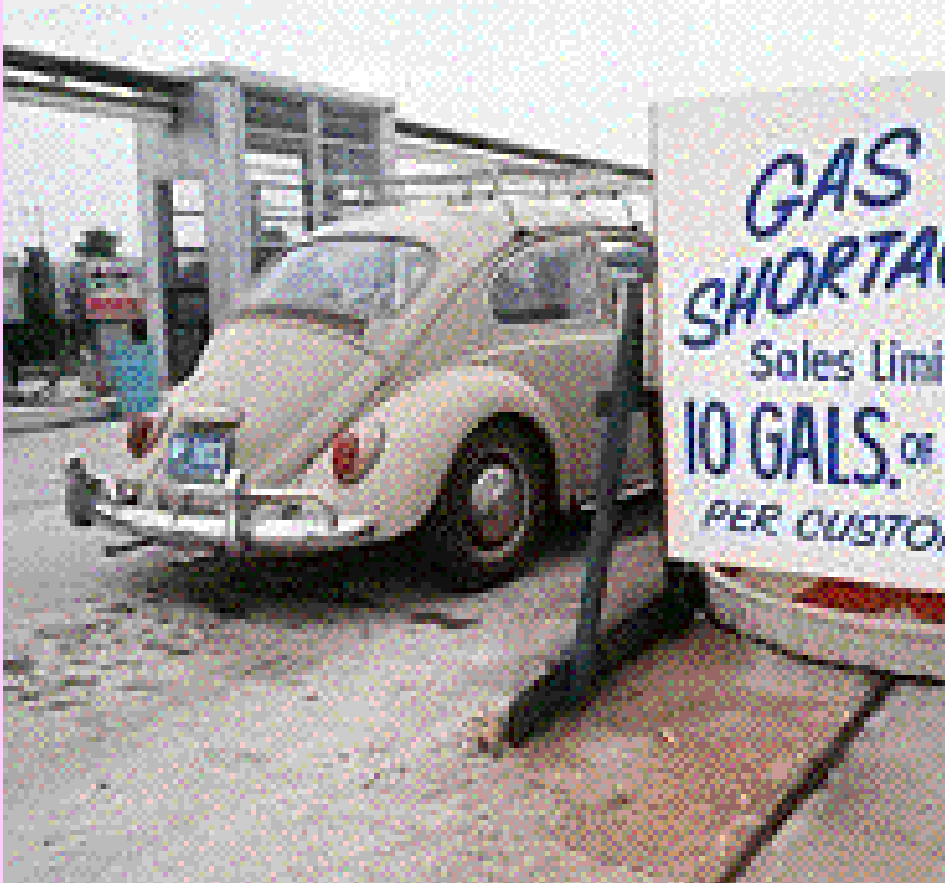
# *Let's even bring in Alan Greenspan*



**and his  
colleagues at  
the Federal  
Reserve**



# Usual View



**Shortages are Bad Things**



# Usual View



**Shortages are Bad Things**

# Usual View



Photograph by Joe Munroe/Ohio Historical Society Collections

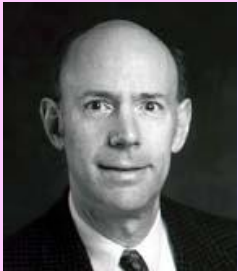
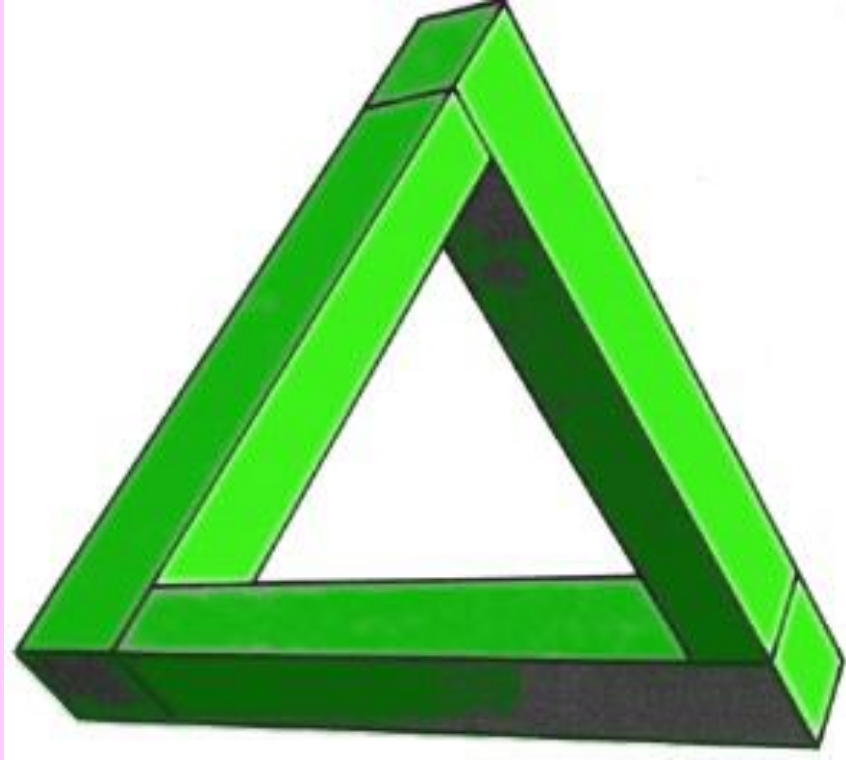
**Surpluses are Bad Things**

# Usual View



**Surpluses are Bad Things**

# Our View



**Shortages can be**

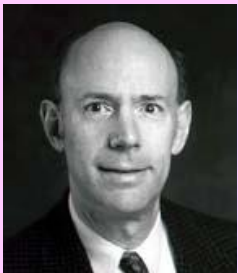
***Good Things***



**because they can help  
avoid surpluses which are  
Bad Things**



# Example: Nurse Shortage Avoids Nurse Layoffs at UCLA

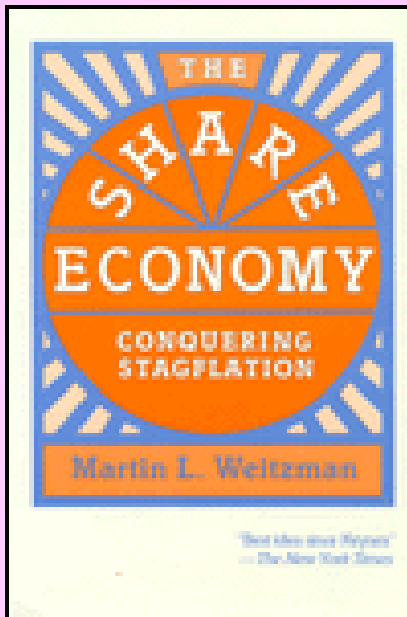


**Shortages can be  
*Good Things***



**because they can help  
avoid surpluses which are  
*Bad Things***

**Idea: Create a labor shortage to  
lower unemployment and  
dampen the business cycle.**



**Labor gets a  
percentage  
share...**



**...instead of a  
fixed wage.**

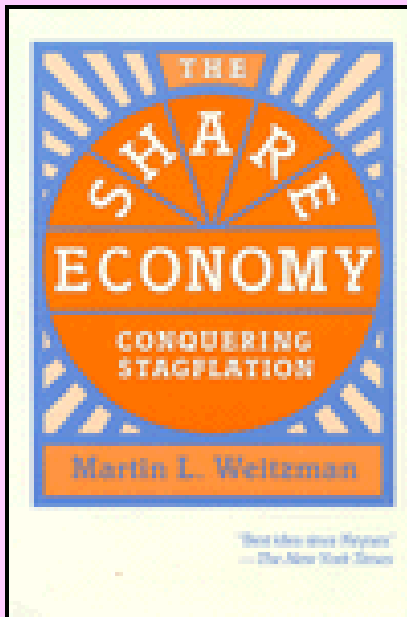
***Martin Weitzman's  
"Share Economy" (1984)***

*But let's also bring in Arnold Schwarzenegger's favorite economist and his "no free lunch" idea*



**If labor market monopsony has a plus side by creating shortages, it also has a minus side.**

**Idea: Create a labor shortage to  
lower unemployment and  
dampen the business cycle.**



**You get the  
share  
economy...**



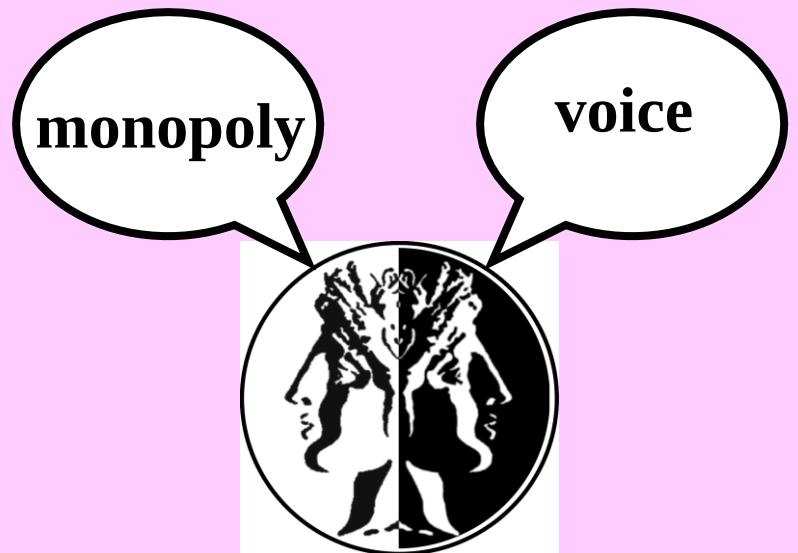
***...without the  
share!***

***Martin Weitzman's  
"Share Economy" (1984)***

# Richard Freeman and James Medoff



## The Two-Face Model of Unions

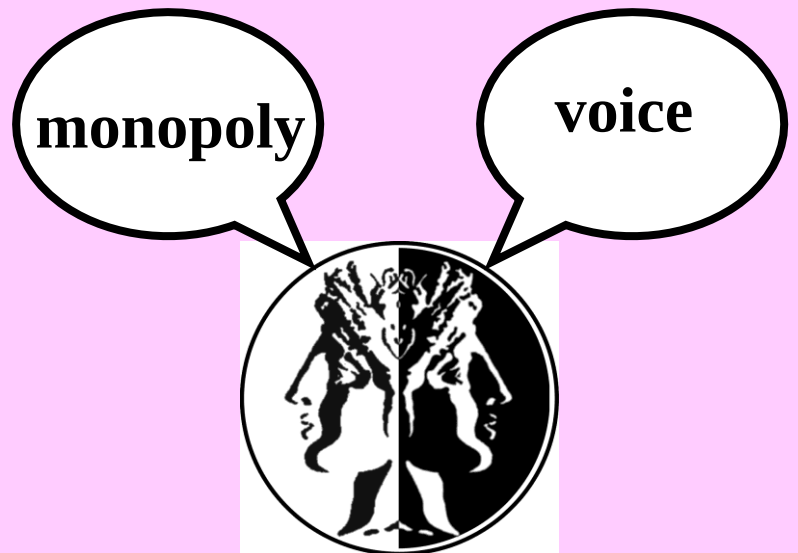


***What Do Unions Do? (1984)***

# Richard Freeman and James Medoff



## The Two-Face Model of Unions



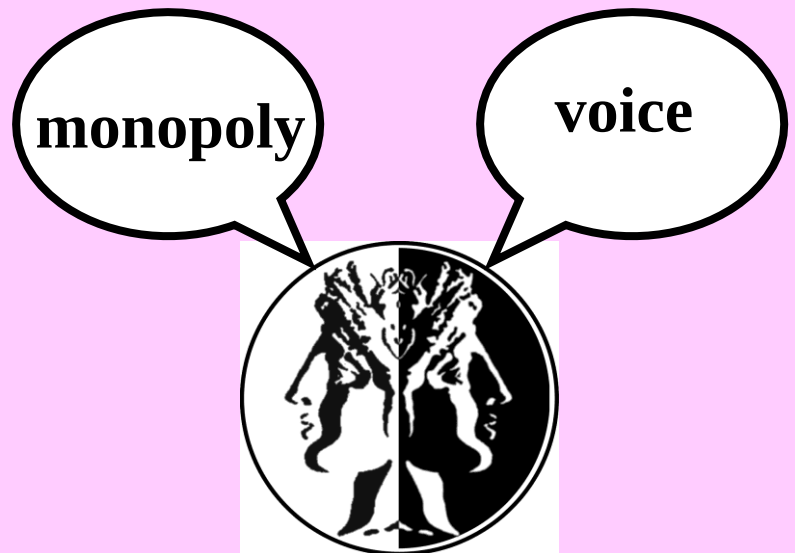
*Note F-M's assumption that opposite of monopoly is textbook "competition."*



# Richard Freeman and James Medoff



## The Two-Face Model of Unions



*F-M: Unions are “inefficient” due to monopoly effect but may make up for that inefficiency by providing productivity-enhancing voice that nonunion employers lack.*





# Mitchell and Erickson *(and U.S. labor law)*

“Inequality of bargaining  
power” is basis of the  
1935 Wagner Act



Not  
competition  
but  
monopsony

reduced  
voice,  
pay,  
benefits



*What Do Nonunion  
Employers Do?*

***The inequality of bargaining power between employees who do not possess full freedom of association or actual liberty of contract and employers who are organized in the corporate or other forms of ownership association substantially burdens and affects the flow of commerce, and tends to aggravate recurrent business depressions, by depressing wage rates and the purchasing power of wage earners in industry and by preventing the stabilization of competitive wage rates and working conditions within and between industries.***



# **Preamble to 1935 Wagner Act**



# Wagner: *Underconsumption*



❑ Small federal govt.  
and pre-Keynes

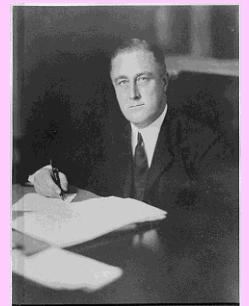
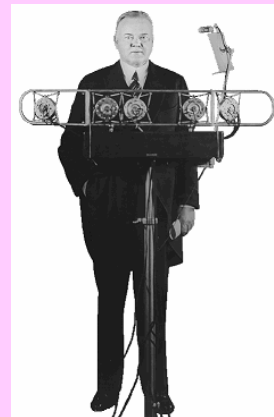


❑ Uncertain role of  
central bank



❑ Widespread view:

- Marx
- Hoover
- Roosevelt



# *Wagner and Pre-Wagner Assumptions*

---



## ❑ Opposite of union labor market is monopsony, not textbook competition



- Monopsony undermines laissez-faire assumption that compensating wage differentials, etc., will lead to optimal balancing of worker & employer preferences
- Absent regulation, insufficient benefits, safety, security, voice, as well as too-low wages, increased wage inequality

## ❑ Nonunion monopsony has macro significance

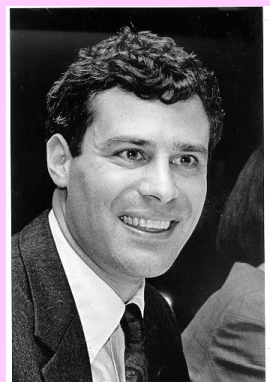
- Wagner View: Underconsumption
- Erickson & Mitchell: Lower NAIRU

# David Card and Alan Krueger



*Nonunion  
monopsony  
applied in micro  
context to the  
minimum wage*

*Why not apply it  
more generally to  
the rest of the  
labor market?*





# *Monopsony, not demand=supply, is norm for “competitive” (nonunion) labor markets*

Figure 1: Turnover Rate Function

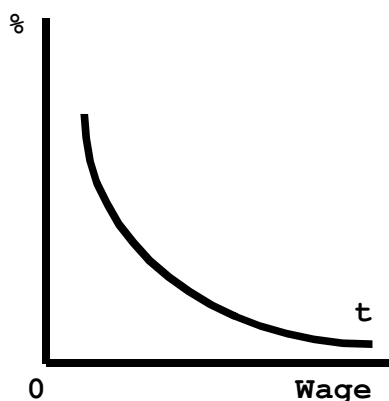


Figure 2: Turnover Number Function

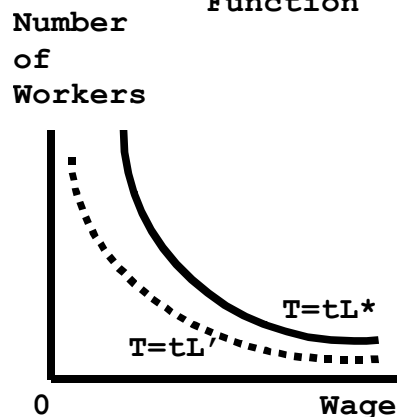


Figure 3: Hiring Function

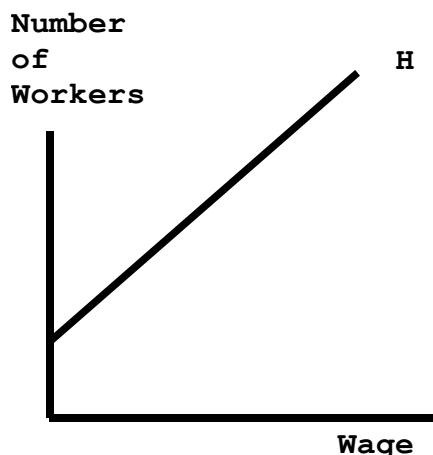
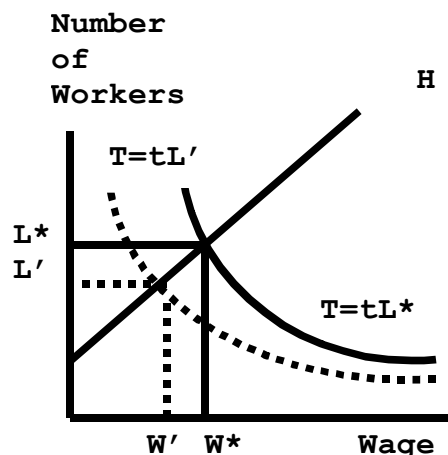


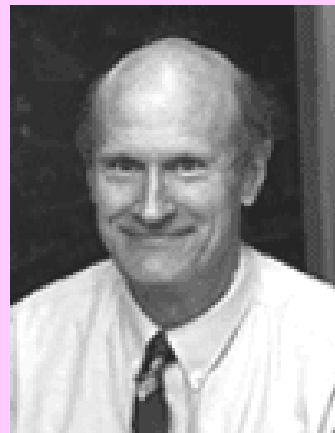
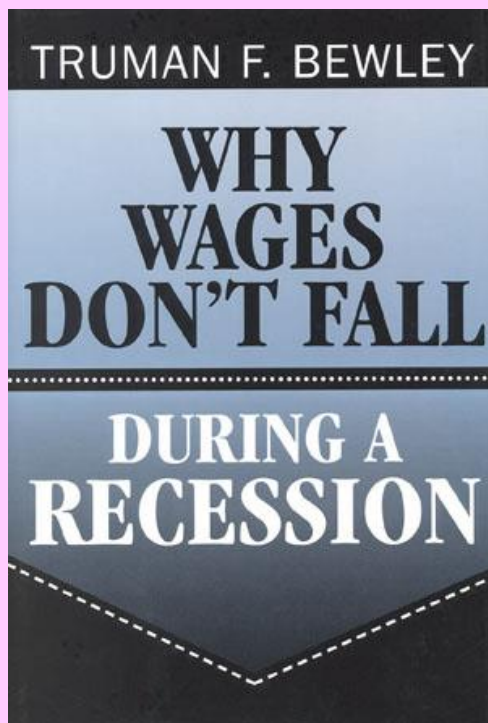
Figure 4: Steady State



Higher wage → bigger workforce, i.e., upward-sloping supply curve

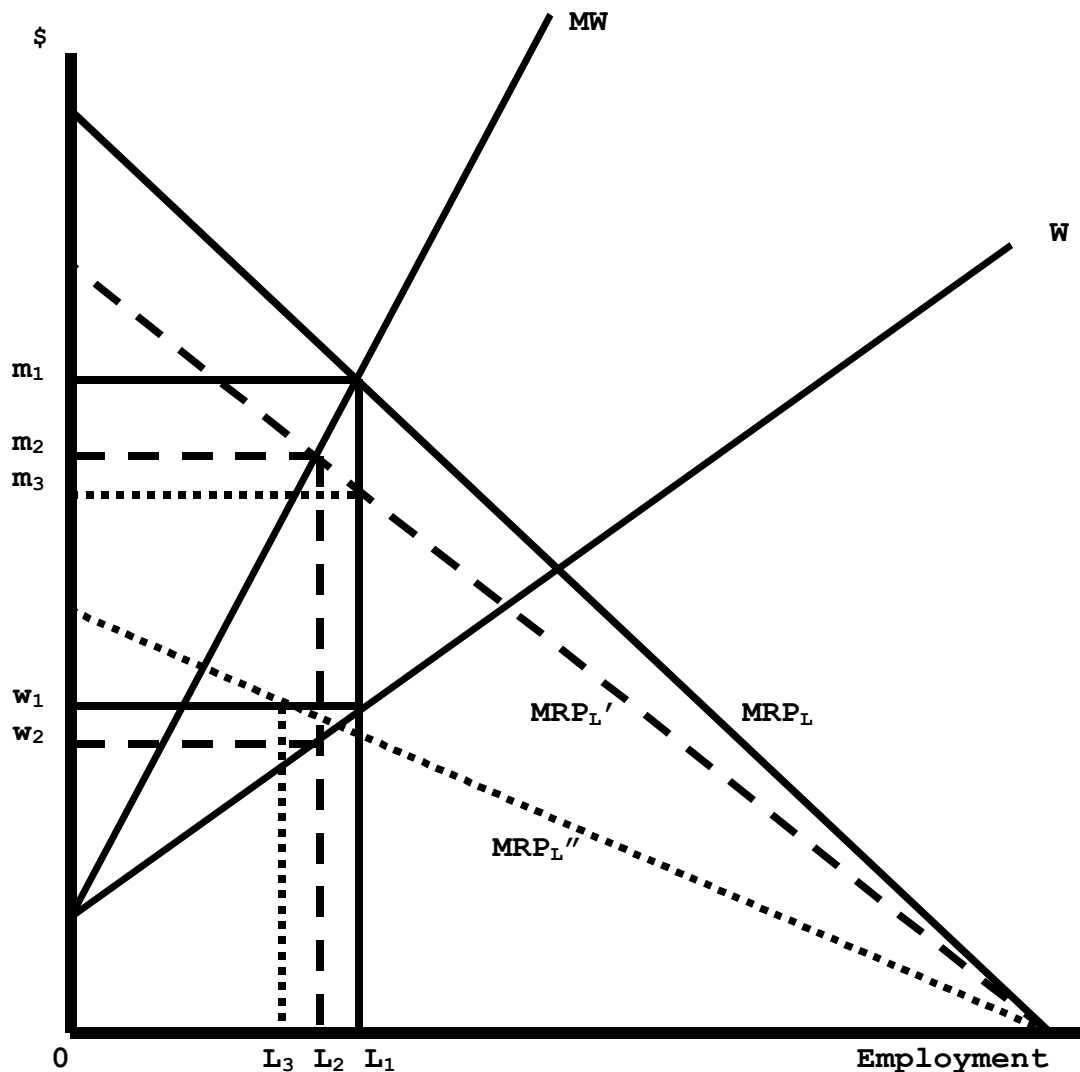


**Combine the  
Card-Krueger  
monopsony with  
downward  
nominal wage  
rigidity**



# *Monopsony, not demand=supply, is norm for “competitive” (nonunion) labor markets*

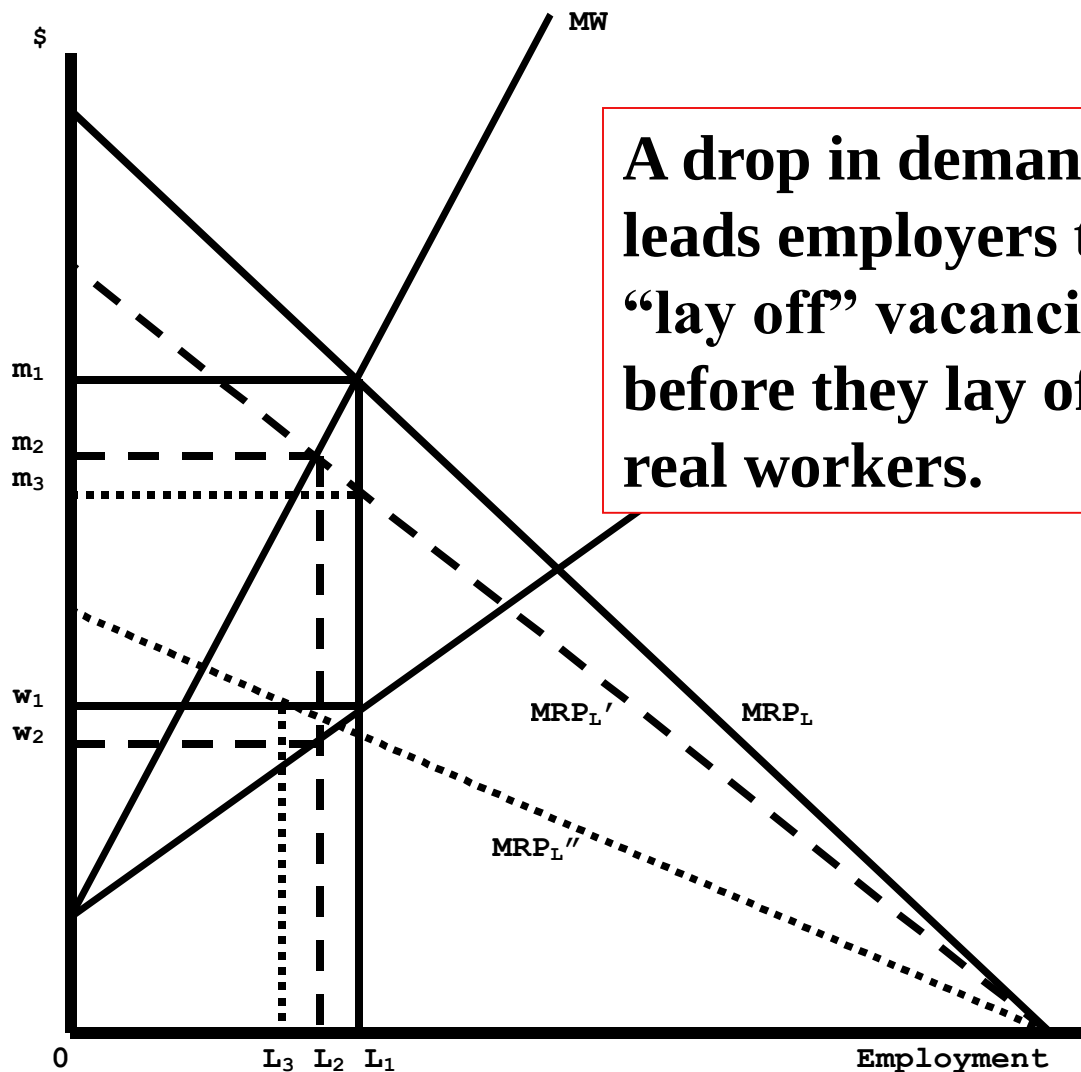
Figure 5: Monopsony With Demand Decline



**Add wage nominalism (downward wage rigidity) to monopsony model**

# *Monopsony, not demand=supply, is norm for “competitive” (nonunion) labor markets*

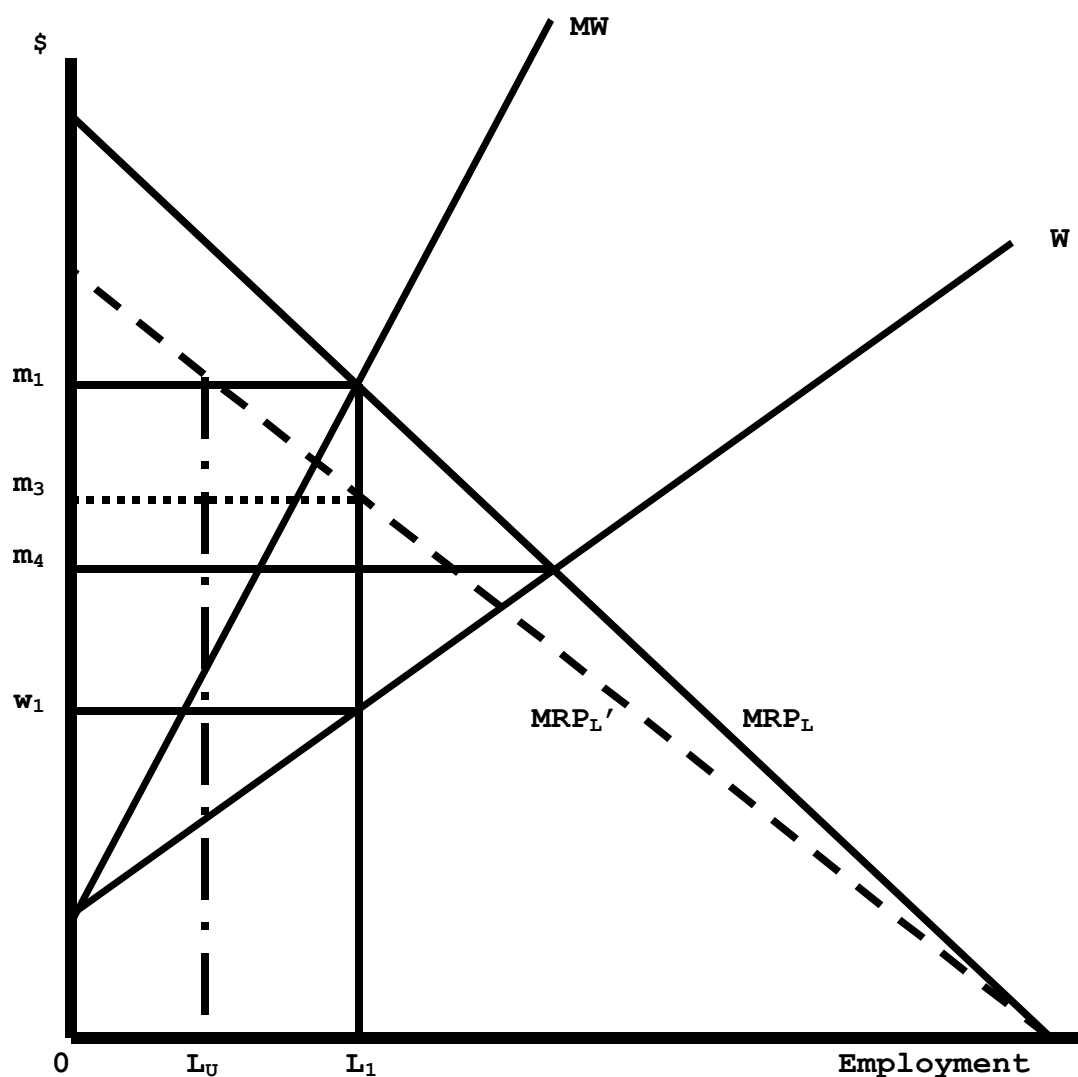
Figure 5: Monopsony With Demand Decline



**Add wage nominalism (downward wage rigidity) to monopsony model**

# *Monopsony, not demand=supply, is norm for “competitive” (nonunion) labor markets*

Figure 6: Union Wage Setting With Demand Decline

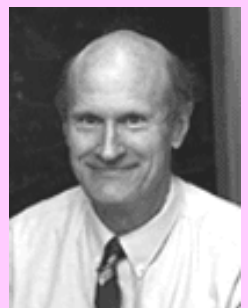
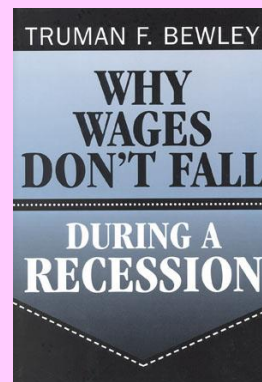
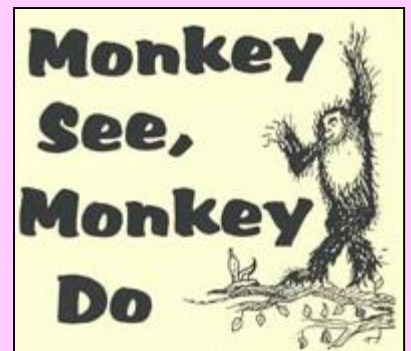
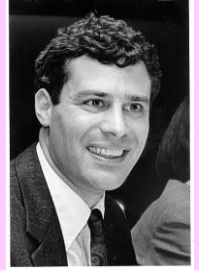


**If union bargains for wage  $> m_4$  (such as  $m_1$ ) and holds it, demand drop leads to immediate layoffs.**

# *Why Monopsony?*

---

- ❑ Flow model  
similar to Card-Krueger
- ❑ Benchmarking,  
a.k.a. copying  
what others are  
doing
- ❑ Risk associated  
with downward  
nominal wage  
rigidity



# *A Wagnerian Moment*



**Die Walküre:  
Siegmond meets Sieglinde**



*Says who he isn't,  
rather than who he is*



# *A Wagnerian Moment*



**Not saying business cycle is dead.**

**Not even saying all recessions will  
henceforth be mild.**

**Not saying that good macro policy  
doesn't matter and that all changes in  
macroeconomics are due to changes in  
the labor market**



# **Historical Source Material:** *Documents at Reagan Presidential Library*



*and memoirs of various  
policy makers*



**Martin  
Feldstein**

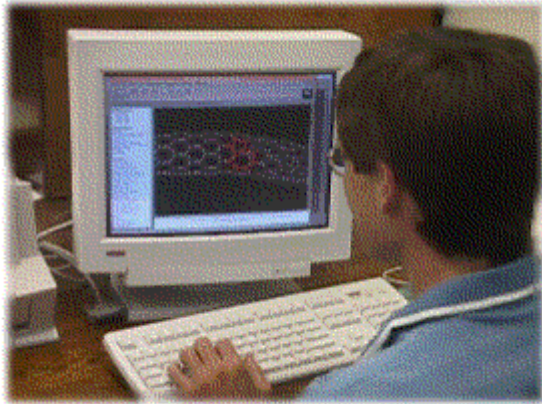


**Murray  
Weidenbaum**



**William  
Niskanen**

# Historical Source Material: *Federal Reserve Transcripts*



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### Schedule of Meetings, Statements, Minutes, and Transcripts

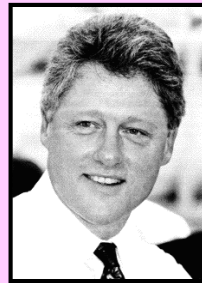
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 The Federal Reserve Board

## Federal Open Market Committee

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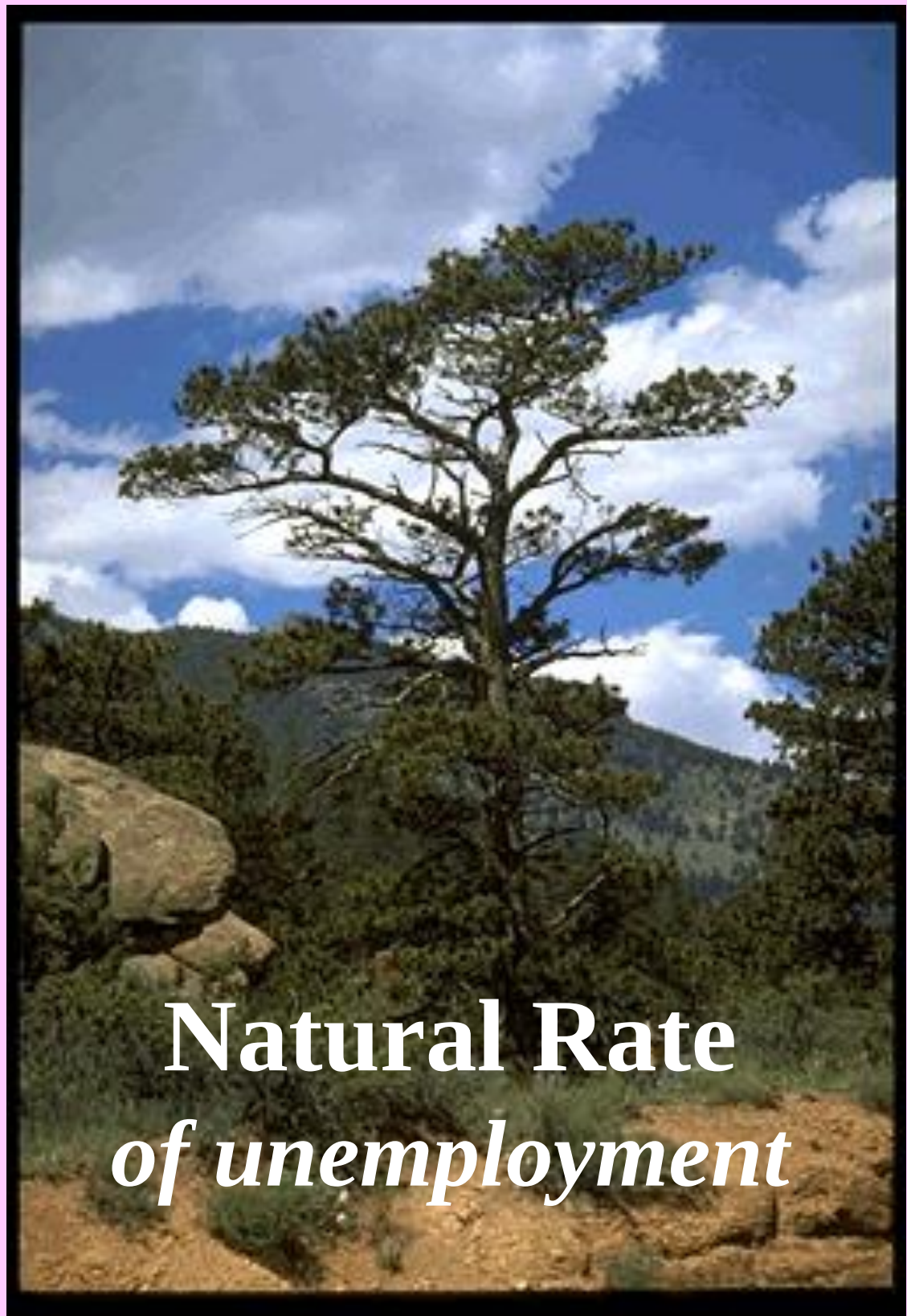
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**Minutes**

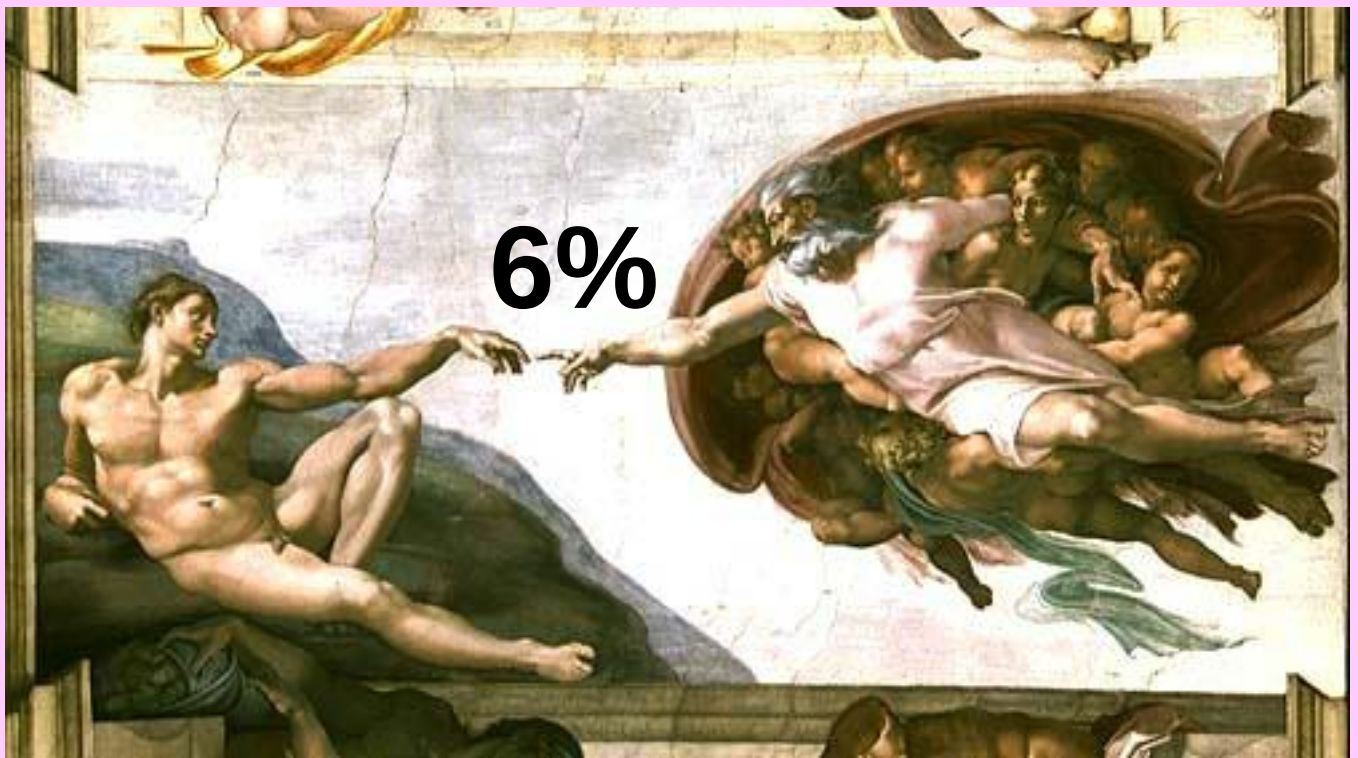
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Natural Rate  
*of unemployment*







6%

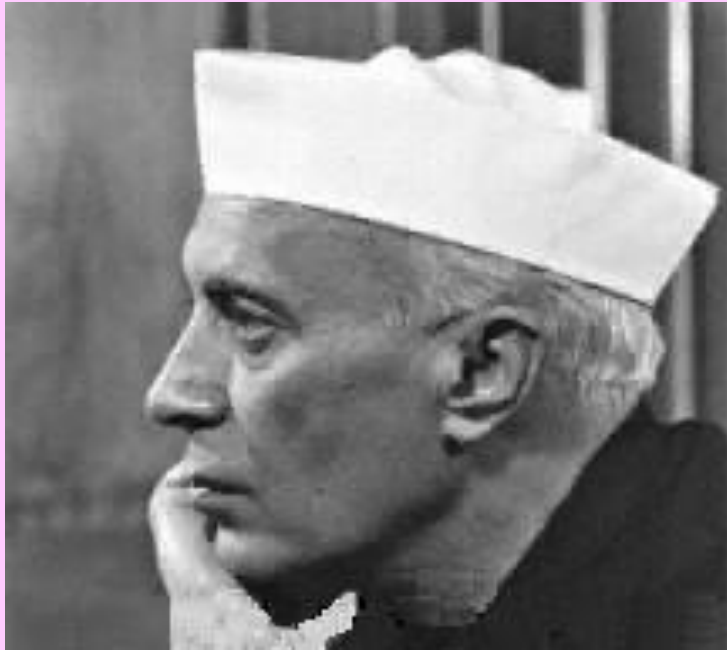
4%

# ***Non-Accelerating Inflation Rate of Unemployment (NAIRU)***





**Not to be confused  
with...**



**Nehru**

# Reagan Fires Air Traffic Controllers: 1981



*Volcker thought it was  
significant*



# NOT YET DEAD AT THE FED



*"The air traffic controllers' confrontation with President Reagan set in motion a fundamental change in policy for this country more than 15 years ago. It is conceivable that we will look back at the UPS strike and say that it, too, signaled a significant change."*

**Alan Greenspan at FOMC  
in 1997 (!)**





# Summing up...

- Employer ascendancy has costs in terms of wage inequality and erosion of employer-based social insurance.
- *At the macro level, you get the “share economy” but without the share.*
- On the other hand, employer ascendancy lowers the NAIRU and creates a cushion against recession...
- *...even if the Fed is slow to understand this change in the labor market.*
- Senator Wagner et al were right: A competitive labor market is in fact monopsonistic.



# *Implications of the “New” Model of Employer Ascendancy*

**IIR  
Berkeley**



**Sept.  
2005**



**Daniel J.B. Mitchell  
and**



**Christopher L. Erickson**